



Office of Inspector General  
**Semiannual Report  
to the Congress**


April 1, 1997 -  
September 30, 1997



**Integrity**

**Accountability**





About our cover:



Office of Inspector General  
(OIG) executives identified the  
five core values depicted on the cover  
at a senior management team-building  
conference held in January 1997.  
We believe these values are essential  
to the success of the OIG. We are  
committed to maintaining these values  
in all aspects of our work at the  
Federal Deposit Insurance Corporation.

---

The FDIC seal is modeled after the seal of the Department of the Treasury, first designed in 1778.

The original design of the Treasury seal contained an abbreviation of the Latin inscription “Thesauri Americae Septentrionalis Sigillum,” signifying “the Seal of the Treasury of North America.”

In FDIC’s seal, the Latin inscription was replaced with the name of the Corporation, and the date 1933 was added to depict the year in which the Congress created the FDIC. The modified seal appeared on the cover of the Corporation’s first *Report of Operations*, issued on March 31, 1934. The seal then and now contains balanced scales to represent justice, a key to symbolize authority, and a chevron with 13 stars to represent the original states.





## Inspector General's Statement

The Federal Deposit Insurance Corporation (FDIC) has a long history of successfully dealing with enormous challenges. The Congress first created the Corporation as part of the Banking Act of 1933 to maintain stability and public confidence in the nation's banking system. The agency was formed in response to the wave of bank failures at the onset of the Great Depression—certainly one of the most troubling and difficult times in the nation's history.

During its more recent history, from 1980 through 1994, FDIC managed the failures of 1,617 banks. In 1988, the insurance fund suffered a loss of \$4.2 billion, the first operating loss in its 55-year history. The later 1990's marked a time of rebuilding for FDIC and the banking industry and continued to present great challenges. FDIC succeeded in liquidating nearly \$317 billion in assets from the failed banks. By 1996 commercial banks earned a record \$52.4 billion. Return on assets averaged 1.19 percent, considered a high level of performance. In 1996, only 5 banks and 1 thrift failed. By year-end 1996, the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) combined totaled \$35.8 billion. No failures have occurred since August 1996 and mid-year 1997 BIF and SAIF combined totaled \$36.5 billion—the largest reserves in the Corporation's history. Given such success, the Corporation has more recently been able to shift its focus from handling and resolving failed institutions to monitoring and assessing existing risks in insured financial institutions.

Notwithstanding these past and ongoing successes, FDIC still faces several challenges as it moves forward. In a sense, the historical challenges of the past have given way to more contemporary challenges brought about largely through corporate downsizing and the complexities of the new technological era in which we live.

FDIC's staffing levels peaked in mid-1993 at 15,611. Its staffing totaled 9,789 at the end of December 1995 when it inherited approximately 2,000 people from the Resolution Trust Corporation (RTC) at its sunset. Through a number of downsizing processes—buyouts, office consolidations, out-placement efforts, and reductions-in-force, as of September 30, 1997, corporate staffing had decreased to 8,044 employees. By year-end 2000, the Corporation anticipates a staff of about 6,500-6,600. When one considers that as each employee departs, a degree of talent, skill, and expertise is lost, the impact of the downsizing on the Corporation's daily work is quite great. Add to this type of loss the fact that approximately 1,100 members of the current workforce are or will be eligible for retirement or "early out" within the next 9 months and other challenges arise. The Corporation will need sufficient, well-trained staff in place to help ensure the continued safety and soundness of federally insured depository institutions. The banking industry is an ever-changing, modernizing environment, and staff will need to address emerging risks in the industry before these risks become serious problems. Newer, less experienced staff members will need to build on the knowledge that served their predecessors so well in dealing with past events to handle new challenges that arise.

---

One known area of challenge that they will surely face is a technological one. More and more the Corporation's workforce is relying on new technology to accomplish the FDIC mission. While certainly not a tool of the 1930's, today automated systems are absolutely vital in carrying out the Corporation's work. FDIC is spending several hundred millions of dollars yearly to identify, develop, and implement new information technologies that it hopes will improve the effectiveness and efficiency of all aspects of the Corporation's primary activities. All the while, the Corporation must ensure that it is adhering to established systems development processes, and that decision makers act wisely as they plan and implement costly technological initiatives.

A pressing concern in the information systems area is the Year 2000 issue. That is, FDIC must ensure that all corporate automated systems are Year 2000 ready. It must also address the necessary steps that vendors and financial institutions must undertake to resolve problems associated with the impending century change date. Toward this end, the FDIC Chairman established an oversight committee to oversee the management and implementation of all of FDIC's internal and external Year 2000 activities. A critical challenge for the committee will be to ensure that plans to address the Year 2000 problem are successfully and timely implemented. We are continuing to monitor the Corporation's Year 2000 efforts and report on its progress later in this document.

The Government Performance Results Act of 1993 is an important piece of legislation that will also impact the Corporation as it goes forward. The Act requires the Corporation to prepare a Strategic Plan that broadly defines its vision and an Annual Performance Plan that translates the vision and goals of the Strategic Plan into measurable objectives. The Corporation recently published a plan that lays out its vision and articulates goals for all of its programs and activities. The plan provides a challenging blueprint for the Corporation to build upon from 1997 through 2002, and FDIC will be accountable for achieving anticipated results. The Corporation needs to continue to address the challenge of developing more outcome-oriented performance measures, establishing effective processes to verify and validate performance measurement data, and integrating program evaluations into the planning cycle.

Who plays the key role in moving the Corporation ahead as it works through the challenges it faces? Certainly, FDIC management must take the lead. Managers must effectively oversee and maintain strong internal controls in their programs. This is a role that FDIC management has taken seriously. It has implemented corrective action in response to a number of Office of Inspector General (OIG), U.S. General Accounting Office (GAO) and other audit recommendations. Additionally, the Corporation's Office of Internal Control Management (OICM) recently sponsored a corporate-wide symposium on internal controls, designed to heighten management's understanding of risk areas and emphasize the value and importance of strong internal controls. OICM has also recently published its final version

of *Audit Coordination and Resolution Guidelines*, which outlines for corporate management the processes and time frames for responding to audit reports issued by the OIG and others.

The Corporation's Audit Committee also continues to play a critical role in giving high-level corporate attention to OIG, GAO and other audit findings. One of the Committee's principal functions is to monitor the internal control systems of FDIC. Monthly Audit Committee meetings have been particularly helpful in providing an opportunity for dialogue between the OIG and senior FDIC management. During the reporting period, the OIG submitted 79 reports for consideration at meetings, and presented 11 of those orally. As discussed later in this report, in several instances, the Audit Committee has requested that management follow up on weaknesses reported by the OIG in an effort to avoid future losses, damages, or recurrences. I appreciate the Committee's support in dealing with issues of concern to the OIG.

One area of concern, which we discuss in detail in the Major Issues section of this report and which we have addressed in past semiannual reports, relates to what the OIG views as a serious vulnerability in the Legal Division's controls over outside counsel billings. We recently met with members of the Audit Committee and FDIC's General Counsel to address a number of issues relating to the Legal Division's responsiveness to OIG findings. We believe our discussion at that meeting will lead to future progress in resolving existing differences.

Another key participant in helping to ensure the Corporation's success is the OIG itself. To that end, our work over the past 6 months has resulted in \$17.3 million in total actual/potential monetary benefits. We have issued 69 audit and evaluation reports over the past 6 months. Of the \$8.6 million questioned in these reports, management has agreed that \$7.9 million should not have been charged to the Corporation. We have also made over 110 nonmonetary recommendations to improve corporate operations and programs, and management has agreed to take necessary actions to address these recommendations. We issued 25 reports on expiring contracts that FDIC assumed at RTC sunset, in which we identified \$4.1 million in questioned costs. Our investigations resulted in 9 convictions, 16 indictments/informations, and \$4.6 million in fines, restitution, and monetary recoveries. We have also engaged in a number of successful cooperative efforts with FDIC management over the past 6 months, among those: providing feedback to developers of the Corporation's new Time and Attendance reporting system on system design and user requirements and working with the Division of Resolutions and Receiverships and Division of Finance to recover delinquent monies owed by former RTC contractors and court appointed receivers.

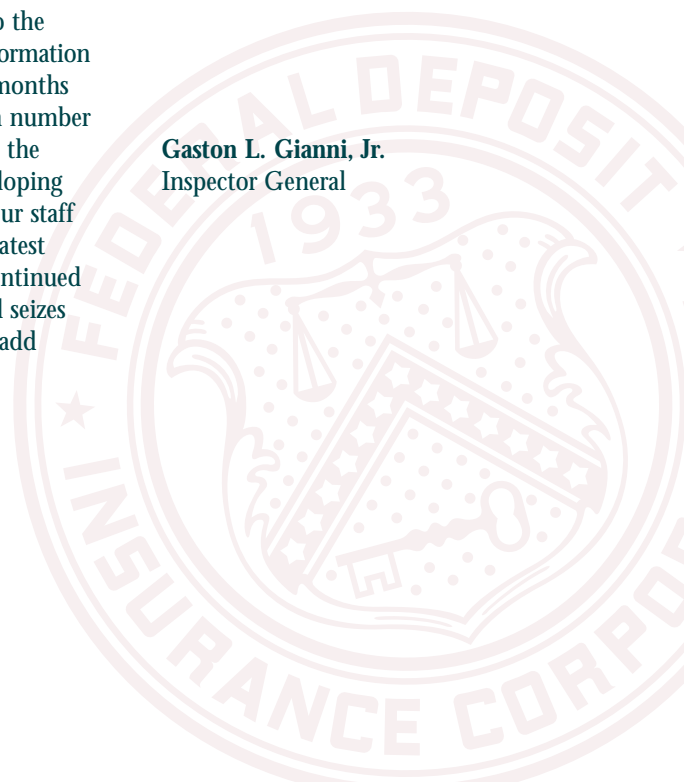
As the OIG moves forward, we continue several important internal initiatives related to our role as an independent audit and investigative entity. We submitted and the Congress approved an appropriated budget for fiscal year 1998. This appropriation is the OIG's first appropriation. The \$34.7 million fiscal year 1998 budget is funded through BIF, SAIF, and the FSLIC Resolution Fund, like other FDIC activities, and represents about 2 percent of estimated corporate expenses. The budget is also about 13 percent less than the 1997 OIG budget, which the FDIC Board of Directors approved as a part of the Corporation's annual operating budget. Similar to other FDIC functions, the OIG has downsized its activities as the thrift and banking crisis has been resolved. I want to thank Members of the Congress for their support of the OIG in approving our budget.

The OIG is also taking steps to more fully assume the personnel and contracting authority afforded us under the Inspector General Act, and we are handling requests pertaining to the OIG under the Freedom of Information and Privacy Acts. During the months ahead, we will further pursue a number of plans designed to "reinvent" the OIG. I am committed to developing the talents and knowledge of our staff so that the OIG makes the greatest possible contribution to the continued success of the Corporation and seizes every available opportunity to add value to the FDIC.

In closing, I will speak to a final, essential key to the Corporation's success—its Chairman. During the past 6 months, Acting Chairman Andrew Hove has served in an interim capacity as Chairman of the Corporation. Chairman Hove deserves much credit for leading the Corporation at this time of transition and for helping to craft FDIC's vision for the future. As of the date of publication of this report, Ms. Donna Tanoue had been nominated to serve as the next Chairman of FDIC. I hope the Congress will confirm the next Chairman as quickly as possible. In this manner, the Corporation will be provided the stability and sustained leadership it needs to tackle the difficult issues ahead and even exceed its past levels of success.

I look forward to working with the next Chairman and all others at FDIC in a spirit of cooperation as we face upcoming challenges and strive to maintain the present stability and public confidence in the banking system.

**Gaston L. Gianni, Jr.**  
Inspector General



## Table of Contents

<b>1</b>	<b>Inspector General's Statement</b>
<b>5</b>	<b>Results in Review</b>
	<b>Major Issues</b>
<b>6</b>	Need for Improved Controls Over Outside Counsel Billings
<b>11</b>	Controls Over Contracts and Agreements are Crucial
<b>14</b>	Asset Management and Liquidation Continue to Pose Challenges
<b>17</b>	Supervisory and Regulatory Activities are Key to FDIC's Success
<b>19</b>	Corporation Must Carefully Evaluate Future Information Technology Needs
<b>22</b>	Difficult Personnel and Downsizing Issues Must Be Addressed
<b>26</b>	<b>Investigations</b>
<b>36</b>	<b>OIG Organization</b>
<b>44</b>	<b>Reporting Terms and Requirements</b>
	<b>Appendices</b>
<b>45</b>	I. Statistical Information Required by the Inspector General Act of 1978, as Amended
<b>59</b>	II. Reports Issued by Office of Congressional Relations and Evaluations
<b>60</b>	III. Statistical Information Related to OIG Completion of RTC Contractor Reviews
	<b>Tables</b>
<b>37</b>	1. Significant OIG Achievements
	<b>Figures</b>
<b>27</b>	1. Fiscal Year 1997 FDIC OIG Investigations by Type
<b>40</b>	2. Office of Inspector General Staffing (1994-2002)
<b>42</b>	3. Reports Issued and Investigations Closed
<b>42</b>	4. Questioned Costs
<b>42</b>	5. Fines, Restitution, and Monetary Recoveries
<b>43</b>	6. FDIC Management Actions on OIG Monetary Benefits



- Office of Audits and Office of Congressional Relations and Evaluations issue a total of 69 reports with questioned costs of \$8.6 million. Management disallows \$7.9 million.
- OIG investigations result in 9 convictions, 16 indictments/informations, and over \$4.6 million in fines, restitution, and monetary recoveries.
- Office of Quality Assurance and Oversight issues 25 reports on expiring Resolution Trust Corporation (RTC) contracts with \$4.1 million in questioned costs.
- OIG staff reviews 20 proposed federal regulations and 39 FDIC directives/manuals.
- OIG takes proactive role in assisting the Corporation by commenting on draft versions of the Strategic Plan being prepared for the Congress and the Office of Management and Budget.
- OIG nears completion of Assistance Agreement work. Of over \$315 million questioned by the OIG during the past 8 years, the Corporation has recovered over \$202 million.
- OIG evaluates FDIC's methodology for identifying FDIC information technology that is not Year 2000 compatible.
- OIG engages in cooperative effort with management to recover delinquent monies owed by former RTC contractors and court-appointed receivers. Recoveries to date total \$1.1 million. Plans are underway for remittance of \$1.3 million more.
- OIG participates with management on a number of projects, including: examining FDIC headquarters' current and future building space needs and options for meeting those needs; providing feedback to developers of a new Time and Attendance Processing reporting system; participating on FDIC's Cost Benefit Analysis Task Force; working with Legal Division to define controls necessary in electronic timekeeping and billing systems.
- OIG carries out significant OIG internal management initiatives, including: OIG Hotline awareness program; world wide web home page on FDIC Intranet; program to test and evaluate the use of automated audit workpapers; issuance of OIG Information Technology Plan; issuance of recommendations on the OIG's awards program; and assessment of OIG management information systems and testing to ensure Year 2000 compliance.

## Major Issues

Need for Improved Controls  
Over Outside Counsel Billings

Controls Over Contracts and  
Agreements Are Crucial

Asset Management and Liquidation  
Continue to Pose Challenges

Supervisory and Regulatory Activities  
Are Key to FDIC's Success

Corporation Must Carefully Evaluate  
Future Information Technology Needs

Difficult Personnel and Downsizing  
Issues Must Be Addressed

### Need for Improved Controls Over Outside Counsel Billings

FDIC and the Resolution Trust Corporation (RTC) have been among the largest federal and even corporate users of outside counsel. According to RTC's former legal information system, the Corporation would have paid over \$1.6 billion in fees and expenses to outside counsel by sunset. As for FDIC, through the end of 1996, the Corporation had paid \$1.3 billion to outside counsel. The Legal Division estimates that it will spend approximately \$64 million during 1997 and \$58 million during 1998 for outside counsel services.

When FDIC and a law firm agree to the legal services to be provided, both parties execute the Legal Services Agreement (LSA) which, along with the policies contained in the applicable Guides for Outside Counsel establish the billing requirements. Generally, LSAs contemplate payment for services on the basis of time expended by attorneys, for which they are entitled to charge agreed-to hourly rates. Presumably, those hourly rates reflect the mutual understanding of FDIC and the firm as to the "value" of the services to be rendered. In effect, FDIC is "buying time" from these firms. Thus, documented support for attorney time charges, usually consisting of attorney time sheets, is central to any evaluation of payment for the performance of services under the LSA. The Guides for Outside Counsel have required that firms must retain copies of all bills and underlying documentation, including original time sheets and other time and expense adjustment records for 3, and when specified, 4 years after payment.

### OIG Questions Unsupported Costs

The OIGs at RTC and FDIC have conducted a combined total of 236 legal fee bill audits over the past 8 years. The OIG's audits are designed to determine whether the fee bills submitted by the firms present fairly the expenses and activities of the cases for which the fee bills were submitted. The OIG reviews contractor claims to determine whether they are adequately supported by source documentation, prepared in accordance with applicable FDIC or RTC governing agreements, and representative of the cost of services and litigation that have been approved in advance by FDIC or RTC.

Those audits have questioned millions of dollars related to fees that were not adequately supported with original time records. We have found that questioned costs from unsupported professional fees generally fall into two broad categories. First, the firms cannot provide all of the professionals' handwritten original time sheets to support the fees billed to the Corporations. Second, the firm either cannot provide the automated time sheets or relevant alternative documentation to support the fees charged or the information generated by the automated timekeeping system cannot be relied upon because of certain internal control weaknesses.

The OIG has vigorously asserted over the past 6 years at RTC and 2 years at FDIC that the Corporation is more vulnerable to fraud and abuse when/if law firms cannot or do not provide the required support for their billings and

has recommended that the Legal Division disallow costs when firms do not comply with their LSAs and governing guidance. The OIG's position is that absent reliable supporting documentation for fees charged, the Corporation cannot be assured that it is truly getting the services for which it is paying. The auditors' concerns are for the millions of dollars in fees that are being charged. In the case of RTC, taxpayer dollars involved in the clean-up of the savings and loan crisis were at stake. At FDIC, wasteful spending impacts funds in the Bank Insurance Fund. Given the large dollars in question and the continued use of outside counsel going forward, the OIG believes that the Corporation should insist on sufficient support for fees billed, particularly when the Legal Division's own LSA requires support, and guidance is clear on the requirements for maintaining manually-kept original records. When support is missing, the OIG has no alternative but to recommend that the Legal Division disallow such costs.

---

#### **Legal Division Generally Allows Most Unsupported Time Charges**

In most instances, the Legal Division's position when manual time sheets are missing is not to disallow the full dollar amount of the time charges. Instead, without additional documentation, the Legal Division customarily concludes that value has been received for the services and often bases this view on

the fact that Legal Division oversight staff have reviewed and accepted the bills on a contemporaneous basis. In any case, to serve as a "penalty" for not following the requirements in the *Guide for Outside Counsel*, the Legal Division applies a sliding scale that requires five factors to be considered: the percentage of time charged that is not supported by original time sheets; whether the time sheets located and reviewed as part of the audit revealed any discrepancies between fees billed and those time sheets; whether indications of fraud were uncovered during the audit; the reason the time sheets were unavailable (whether the firm was culpable or "blameless"); and whether the bills not supported by time sheets appear reasonable and represent charges for which the Corporation received commensurate benefits.

The OIG has concluded that the application of the sliding scale is arbitrary and the penalty calculated, if any, is based on subjective judgements and bears little direct relationship to the totality of the unsupported charges that were questioned. The process provides no new credible evidence to specifically support the appropriateness of the charges. Rather, it relies on the fact that some defined service was provided even though the level of effort associated with the service is not supported. We have discussed the issue of unsupported billings in a number of our semiannual reports, and in one report, we showed that for nine recommendations, in applying the sliding scale, the Legal Division allowed \$595,384 questioned and agreed to disallow only \$1,144. Moreover, on eight of the nine recommendations, the Legal Division

was effectively setting a precedent by allowing the full amount questioned by the OIG, thus closing the door on the possibility of negotiating monetary recoveries from these and perhaps other firms.

As more firms continue to convert their manual accounting records to computerized accounting systems, additional issues related to "original documentation" have presented themselves. While the OIG must continue to question any computer generated billings produced from a system with insufficient internal controls, the Legal Division has not agreed to disallow the costs. Instead, it argues primarily that the Corporation has not issued clear guidance to the firms related to internal control requirements for computerized accounting systems. This argument has been offered for the past several years. (Other arguments include that the firm's records are creditable, absent evidence to the contrary; retrieval of handwritten documents is burdensome; computerized records have been reviewed and accepted on a contemporaneous basis; and electronic records are accurate links to original documentation.)

For these reasons and because the Legal Division feels that the electronic media reflects the same entry that would exist from original documentation, they do not challenge the bills in question.

---

#### **Criminal Case Shows Necessity of Support for and Controls Over Legal Fee Billings**

During the reporting period, the OIG assisted the US Attorney's Office for the Southern District of New York and the Federal Bureau of Investigation in a criminal investigation of a Manhattan based law firm that both RTC and FDIC had engaged as outside counsel.



The investigation disclosed that the firm's managing partner defrauded the FDIC and RTC of approximately \$1.4 million in an over-billing scheme where original time sheets had been altered. As a result, the managing partner pleaded guilty to criminal charges of mail fraud, false claims, false statements, and obstructing a federal OIG audit. Also, on August 21, 1997, the United States, the managing partner, and the successor law firm entered into a Civil Settlement and Release under which the partner and firm will pay over \$2.9 million to settle the government's potential civil claims arising from the false billings.

The circumstances of this case dramatically illustrate the serious risks that the Corporation faces in its contracts with outside counsel and the critical need for strong oversight and strict controls over billings submitted by law firms conducting business on behalf of FDIC. At the heart of the case is (1) the alteration and in many cases the later destruction of manually prepared time sheets and (2) computer generated time sheets that were produced by a system that did not have adequate controls in place so that an audit would have been able to detect the fraud that was being perpetrated. This is why the OIG has been steadfast in its insistence that the Legal Division enforce its guidance and require in all cases the support needed to justify both manually and electronically maintained law firm billings.

► **The Scheme:**

The attorneys and paralegals in the firm would record the hours and a description of the work they had done every month. Many used handwritten diaries to record the information. At the end of the month, the hours would be entered onto a computer disk which was then provided to the firm's office manager. The office manager would merge the data in these disks and create a draft monthly bill for the billing partner. In this instance, it was the managing partner referred to above. The draft bill would present the hours worked and the work performed on behalf of the Corporation each day by each attorney.

After receiving the draft monthly bill for FDIC and RTC, the managing partner, using a pen or pencil, made numerous changes to increase the daily hours that had been reported for the firm's attorneys and paralegals, generally increasing the hours by between 1 and 4 hours per day, and sometimes



increasing an attorney's daily hours by more than 4 hours. By deliberately inflating these billable hours, the managing partner was increasing the amount of compensation the firm would receive from the Corporation in return for the supposed services provided. Typically, the changes he made increased the hours billed by the firm in excess of 10 percent each month.

The firm's office manager typed in the upward changes that the managing partner had made by hand. The office manager then prepared a final bill, which was signed by or on behalf of the managing partner and sent to FDIC or RTC. The Corporations would then pay the bills, with occasional minor accounting adjustments. The Corporations were unaware that the hours reported on the bills they received from the firm had been inflated to exceed the hours that the firm's personnel had actually worked.

Over a 26-month period, the scheme continued. In total, the firm submitted bills that requested compensation exceeding by approximately \$1.4 million the amount of money to which the firm was entitled.

#### ► **The Cover-Up:**

In early 1993, the managing partner and his firm were notified that the OIG would be conducting audits of the firm's billings. Before the audits began and during the course of the audits, the managing partner took various actions to conceal from the auditors that he had fraudulently inflated the hours reported on the firm's bills to FDIC and RTC. These steps included collecting

original time records for attorneys, including their handwritten diaries, and having those records destroyed or not produced to the auditors; and causing the firm's office manager to make false statements to the effect (1) that attorneys at the firm had not created handwritten records of their hours and (2) that attorneys at the firm had personally reviewed and approved the portions of the bills sent to FDIC and RTC that described the hours they had worked. Auditors working on the audit did not uncover the fact that the hours that firm personnel had worked had been fraudulently inflated because there were no original time sheets they could check to support the computerized billings.

In fact, the scheme came to light when the US Attorney's Office received a tip that the firm may have cheated the government. Prosecutors opened the criminal fraud investigation, which later culminated in the managing partner's guilty pleas.

This case shows why the OIG has consistently held that the Legal Division must insist that law firms maintain and retain sufficient support for their billings. It also argues for strengthened oversight of billings submitted by the law firms to the Legal Division before payment to the firms is made. The issue of the Legal Division's fee bill review and approval process is the focus of an ongoing OIG audit, and we will report the results of that audit in the next semiannual report.

### **Current Status of Debate Between the OIG and the Legal Division**

In light of the long-standing differences of opinion on these matters, and the fact that, proportionately, more firms are using electronic time and billing systems, the Audit Committee requested that the OIG and the Legal Division jointly undertake a project to identify and define the internal control requirements of electronic time and billing systems used by outside counsel. The OIG and Legal Division have endorsed the following basic internal control features for electronic record keeping. They are consistent with generally accepted auditing standards and available in various software packages:

- Unique identifiers (user identification) and passwords for each user of the system.
- An access profile for controlling user access to each application.
- An audit trail that identifies dates of entry, change, or deletion.
- Information, although not mandatory, that shows the extent of the change or the reason for the deletion.
- Provisions for a user identification code or other certification when the information entered is approved and forwarded for processing of the final fee bill.

The Legal Division has indicated that it intends to include these internal control features as a supplement to the *Guide for Outside Counsel*, making them advisory immediately, and making them fully effective on January 1, 1998. The OIG believes that the Legal Division must be very clear in its insistence that firms use systems that contain such controls.

The OIG also recommends that firms that are either unwilling or unable to invest in software packages with adequate internal control features should maintain original paper copies. Original documentation is already a requirement in the *Guide for Outside Counsel*. The Legal Division, however, believes it should not automatically disallow fees if (1) the electronic system contained an inadequate audit trail; (2) the controls were not adequately implemented; or (3) original paper copies are unavailable.

The Legal Division argues that audit standards for support are very different from professional and judicial standards for assessing and valuing legal services. As a point of departure, the Legal Division now proposes to:

- Consult with professional service firms that review legal bills to see what additional steps might be considered, short of automatic disallowance suggested by the OIG, to seek to improve the initial guidelines for electronic billing and
- Consider the possible use of a liquidated damages provision to cover situations involving the absence of required audit support.

The disagreement over what constitutes acceptable supporting documentation for fees charged by outside counsel has endured over the past several years. By way of issued reports, memorandums

issued to the Legal Division, and discussions before the Audit Committee, the OIG has urged the Corporation to take action on this major issue of concern. We believe the case of the fraudulent overbillings from this reporting period should drive home to the Legal Division the urgency of enforcing clear guidance, insisting on reliable support for time charges billed, and disallowing costs when such support is not provided. The OIG is concerned that in the criminal case cited above, the managing partner in question was, for months, able to get away with never maintaining and/or producing supporting documentation to support his firm's millions of dollars in billings to FDIC. Moreover, the computer system generating the final bills was not adequate to protect the Corporation from a scheme that may have cost it far more than \$1.4 million, had it not been uncovered through a criminal investigation. We would suggest that other similar cases may exist—currently and perhaps indefinitely going undetected. At a recent, special meeting of the Audit Committee, OIG and Legal Division representatives discussed points related to many of the above discussed issues. We also focused our attention on dealing with a current backlog of reports, many of which contain findings related to unsupported billings (See discussion below.) The OIG will continue to pursue with the Legal Division a mutually agreeable resolution of these differences. We believe we are making progress to that end.

### **Other Legal Fee Bill Audit Work**

The FDIC continues to contract with outside law firms to provide a significant portion of the legal services required by the Corporation. The former RTC's carryover legal work has added to the volume of law firms performing work on behalf of the FDIC. About 38 percent of the matters pending as of September 30, 1997, were handled by outside law firms. The FDIC Legal Division projects that \$58 million will be paid to outside law firms in 1998.

During the current reporting period, the OIG issued 27 reports on audits of legal fees paid to various firms. Collectively, these audits demonstrate that the Corporation remains vulnerable to both unintentional and deliberate billing discrepancies. These audits identified questioned costs of \$1,037,915. The audit reports continue to question costs related to unsupported billings, billing errors, unauthorized markups, inadequate descriptions of services provided, excessive time charges, inappropriate staffing, and unsupported or unallowable expenses. A listing of final legal fee bill audit reports issued during the reporting period is contained in Table I.2 of Appendix I.



---

### **Going Forward—Processing and Reporting on Legal Fee Bill Audits**

As noted above, as a result of FDIC's merger with RTC, the OIG's workload included a large volume of ongoing audits of law firms providing services to both Corporations. For each audit, the process of issuing draft reports to the Legal Division, obtaining and resolving comments, and issuing final reports has taken long periods of time, resulting in a large uncompleted backlog of audits. The OIG and Legal Division have been working together to address this backlog.

The OIG has developed new processing and reporting procedures for its backlog of legal fee bill audits. The interim procedures are intended to eliminate the current backlog, ensure that audit results are reported more timely, prioritize the processing of older and larger dollar audits, and make more efficient use of OIG and Legal Division staff resources. As of the end of September 1997, the OIG had 92 active legal fee bill audits.

In those cases where estimated final questioned costs are less than \$100,000, the OIG communicated the results to the Corporation via memorandum. Although the OIG did not issue separate reports per se, we requested that the Legal Division advise the OIG when corrective actions were completed on each of the individual audits.

The OIG then asked the Legal Division to concentrate its efforts on providing us comments for audits containing estimated final questioned costs over \$100,000 that were conducted primarily in 1995 and 1996. The Legal Division devoted additional resources to this work and after 5 weeks provided us with responses to all 16 of those audits, thus reducing the backlog.

The OIG continues to assess the timeliness of the Legal Division's comments for other audits and has reached an agreement with the Legal Division on a schedule for completing management comments for the other audits. Where appropriate, the OIG could issue reports in final without management comments if there is, in the OIG's opinion, undue delay in receiving management response. The timeliness assessment of these remaining audits will consider the draft report issuance date, the law firm response due date, and law firm response receipt date.

These measures are being taken so resources of our respective offices can be more appropriately focused on the more significant high-dollar reports in a more timely manner. As for new legal fee bill audit work going forward, the OIG will incorporate several new features in the audits. Audits will look at 1 year of payments rather than 4 years, and 100 percent of labor charges will be reviewed for authorized personnel and application of appropriate rates rather than 20 to 50 percent. Additionally, our audits will include procedures to determine the causes of findings to better enable us to make conclusions and recommendations regarding the quality of oversight.

---

### **Controls Over Contracts and Agreements Are Crucial**

The FDIC and RTC have relied heavily on the private sector to accomplish the mission of managing and selling assets of failed banks and savings institutions. Over the past 9 years, FDIC and RTC have spent several billions of dollars in contractor fees to assist the Corporation in fulfilling the myriad of time-critical assignments mandated by legislation and the banking and thrift industry crises. Notwithstanding RTC's sunset, FDIC continues to rely on the private sector to accomplish its mission. Projections of 1998 contract awards and purchases total 6,500 contracts valued at \$330 million. Although this is a significant decrease from 1992 when FDIC and RTC collectively spent \$3 billion on contracts, continuing audit coverage is required.

FDIC is also responsible for a number of financial assistance agreements. Generally, assistance agreements have been used as an inducement for investors to acquire failed institutions. Investors acquiring troubled banks and savings institutions receive financial support through such an agreement. Further, an assistance agreement provides protection to the acquiring association or institution against losses incurred for the management and disposition of assets acquired from failed thrifts. FDIC inherited responsibility for administering these agreements from the Federal Savings and Loan Insurance Corporation (FSLIC) with the passage of the Financial Institutions Reform, Recovery and Enforcement Act.

---

The magnitude of contracts and agreements transitioned from RTC and FSLIC and additional contracts awarded by FDIC present significant challenges to the Corporation. Specifically, the goods and services needed by the Corporation must be solicited, competitive bids evaluated, and contracts awarded to the deserving bidder. Throughout that effort, the Corporation also strives to achieve its overall goal of encouraging minority- and women-owned business participation. The challenges continue after the contracts are awarded. During the performance of the contract, the contracts must be monitored, invoices for goods and services have to be paid, and disagreements with contractors have to be resolved. Without proper oversight, the Corporation risks being charged much more for services than it should and funds risk being wasted. As for the assistance agreements, FDIC must be sure that claims for financial assistance are supported and all payments made and credits due are correct.

---

#### **OIG Questions Contractor Billings**

The extensive use of, and reliance on, contractors increase the Corporation's exposure to fraud, waste, and abuse. During its reviews of contract issues, the OIG seeks to lessen the Corporation's exposure and add value to corporate operations. The OIG continues to devote a significant portion of its resources in the area of contract and agreement oversight. During the past reporting period, the OIG issued 16 products related to contracting issues.

These reports questioned \$2.5 million in contractor costs that were billed to FDIC. Additionally, the OIG has been assisting management in its effort to close out expired RTC contracts. Reports issued as part of this endeavor questioned \$4.1 million. The Corporation's Office of Contracts has often been responsive to costs we have questioned, disallowed a significant percentage of these costs, and initiated efforts to recover questioned amounts. Various offices within the OIG have contributed to the overall effort of auditing and reviewing contractors and assisting management in minimizing risks in contracting and assistance agreements activities, as illustrated in the following examples.

The Office of Audits completed an audit of the financial advisory services contract between the FDIC and Wasserstein Perella Mortgage Capital, Inc. and Graves & Associates, Inc. As a result of that audit, the OIG questioned \$701,160. The audit results showed that Wasserstein did not maintain sufficient documentation to substantiate \$684,100 of hourly fees billed to the FDIC under this contract. In addition, \$15,603 for travel costs were paid to Wasserstein that were unsupported or unallowable under the contract. Wasserstein provided adequate support for the \$3 million in asset disposition fees that were charged to the FDIC based on a percentage of net proceeds received from the asset sales. The audit found only minor errors in the calculations of these fees. The audit also disclosed that a significant amount of work was performed on the contract before proper contractual authority was granted.

It was also noted that Wasserstein did not adhere to the Minority- and Women-Owned Business (MWOB) regulations, by using its MWOB joint venture partner, Graves & Associates, Inc., for only 5.6 percent of the work instead of 25 percent as required by the contract. The Associate Director, Acquisition Services Branch, agreed with the findings and recommendations contained in the audit report.

---

#### **Audits of Assistance Agreements**

The OIG completed five assistance agreement-related audits during the reporting period. The most significant findings related to our audit of Bluebonnet Savings Bank, FSB of Dallas, Texas.

Our audit was designed to determine whether Bluebonnet (1) had adequate documentation to support the quarterly claim reports and the settlement payment, (2) had adequate internal controls over the accounts through which assistance transactions were recorded, and (3) complied with the provisions of the assistance agreement and settlement agreement pertaining to the claims for assistance. The scope of this audit specifically excluded tax benefits because all tax benefits due to/from the effective date of the assistance agreement through its termination were settled in the settlement agreement.

During the audit period, Bluebonnet received over \$1 billion of net assistance from the FDIC in addition to a settlement payment of \$77.5 million.

The settlement agreement limited Bluebonnet's obligation to the FDIC as a result of this final compliance audit to \$350,000. Our audit disclosed that Bluebonnet did not produce adequate support for \$708,570 of assistance claims. Also, we were unable to verify that the amount of income due to the FDIC was remitted because of Bluebonnet's inability to produce adequate documentation. For the assistance claims that were supported by documentation, we found errors resulting in overpayments of assistance totaling \$79,262. FDIC management officials have agreed with the OIG's audit results and disallowed \$787,832 of our questioned costs. However, because of the cap on Bluebonnet's obligation, the Corporation only could recover \$350,000. It recovered the maximum amount on October 14.

---

#### **OIG Assists Management in Closeouts of RTC Contracts**

As reported in several of our previous semiannual reports, the OIG's Office of Quality Assurance and Oversight (OQAO) has been assisting FDIC management in an effort to close out 112 expired RTC contracts. Under a Memorandum of Understanding signed in June 1995, OQAO assumed responsibility for completing reviews of expiring contracts that had been initiated by RTC management. These contract reviews are designed to ensure accountability of all assets, accuracy of fees, and the accuracy and allowability of reimbursable expenses paid to the contractors.

#### **OIG Completes Large Volume of Assistance Agreement Work**

FDIC has sometimes used assistance agreements to resolve troubled or failing institutions. Assistance is generally either a one-time cash payment or on-going payments over a period of time to cover losses incurred by the assuming bank on certain assets it took from the failing institution.

The FDIC OIG is nearing completion of its audits of former Federal Savings and Loan Insurance Corporation assistance agreements.

Many of these agreements were for a 10-year period and contained complex terms for determining the amounts of assistance owed. These agreements were considered a very high-risk audit area not only because billions of dollars in assistance were paid to the acquirers, but also because the structure of the agreements themselves offered little incentive to the acquirers to minimize costs to FDIC.

From 1989 through the present, the FDIC OIG has issued 272 reports on assistance agreements and the related tax benefits. Some agreements were terminated or settled early, and the FDIC OIG audited the final payments. In total, for all of the assistance agreement audits, the FDIC OIG questioned over \$315 million. FDIC management agreed with these questioned costs and to date has recovered over \$202 million. Some recoveries are currently being sought through litigation, and total recoveries could rise if litigation is resolved in the FDIC's favor.



The OIG is nearing completion of this effort. During this reporting period we issued 25 reports to FDIC management, containing recommendations to disallow \$4.1 million in questioned costs. These costs were questioned because they were unsupported, unauthorized, or unallowed under the terms of the related contracts. In addition, those reviews identified \$1.61 million in other financial adjustments, such as income from assets that was due FDIC, and open bank accounts that should have been closed, with balances forwarded to FDIC.

Through the end of this reporting period, the OIG has issued a total of 82 reports covering 87 expired RTC contracts. These reports have included a total of \$12.77 million in questioned costs. Management has responded to recommendations in 45 of these reports. In these responses, management has agreed to disallow \$2.96 million of the \$4.22 million (70 percent) questioned.

Currently OQAO has 6 contract reviews in process, which it expects to complete during the next reporting period. No additional reviews are planned. OQAO will also continue to work with management to reach agreement on actions to be taken on all recommendations.

## **Asset Management and Liquidation Continue to Pose Challenges**

Even nearly 2 years after the dissolution of RTC, on December 31, 1995, it is still relevant to speak of the asset inventory that FDIC inherited from RTC. The Corporation continues its work to dispose of remaining assets of insolvent institutions in a timely manner that also maximizes value to the receivership and insurance funds. In fact, marketing and managing assets to maximize value is part of a corporate goal in the receivership management area of FDIC's strategic plan.

Historically, both FDIC and RTC faced enormous challenges in the asset management and liquidation areas when institutions were declared insolvent and their assets were sold or liquidated. From 1980 through 1996, FDIC resolved 1,515 closed institutions with approximately \$243 billion in assets. From 1989 through 1995, the former RTC resolved 747 failed institutions with approximately \$403 billion in assets.

The book value of FDIC assets in liquidation peaked in mid-1992 at \$44.4 billion. As of year-end 1996, they stood at \$8.7 billion - only one-fifth of the 1992 levels - despite \$7.7 billion in RTC assets transferred to FDIC at the end of 1995. About \$4.4 billion of the assets in liquidation at the end of 1996 were those transferred from RTC, and the remaining \$4.3 billion were assets from FDIC liquidations.

FDIC expected to reduce assets in liquidation by approximately 50 percent during 1997 to a level of about \$4 billion. As of August 31, 1997, assets in liquidation totaled \$6.2 billion. It is expected that the majority of the remaining assets, which are the most difficult to sell, will be disposed of by the year 2000. Former Chairman Helfer predicted an asset inventory of \$1.5 billion by year-end 2000.

Although FDIC and RTC have disposed of a high percentage of the assets from financial institutions that have failed since 1980, it will still be some time before the activities of the FSLIC Resolution Fund can be terminated and the savings and loan crisis actually completed. Asset claims administration, assistance agreement management and litigation, and FSLIC and RTC resolution and asset disposition activities will continue to require FDIC management into the future.

Assets have been disposed of through a variety of methods, including auctions, sealed bids, bulk sales, and negotiated sales, as well as ordinary collections. However, because many remaining assets are difficult to sell, FDIC has explored other innovative sales strategies and, at times, has needed to conduct legal reviews and analyses before liquidation could occur.

Given this scenario, FDIC must ensure that it provides extensive oversight for the operation and termination of receiverships, the management of assets owned by receiverships, and the disposition of these assets. With more and more receivership activities consolidated into FDIC's Dallas office, the Corporation has had to ensure proper oversight and monitoring, even though staff are not in close geographical proximity to the assets themselves.

Additionally, FDIC must be cognizant of, and ensure strict adherence to, a number of laws that affect the retained assets. In so doing, the Corporation's efforts can reduce the loss to taxpayers for the thrift clean up and help minimize financial institutions' deposit insurance premiums in the future.

---

### **Review of Securitization Credit Enhancement Reserve Funds**

One method that FDIC and RTC have used to liquidate loan assets is to sell loans in the form of mortgage-backed securities, commonly called securitized loans. A mortgage-backed security is a pool of loans used as collateral to back securities sold to investors in the secondary market. Simply put, principal and interest received from the underlying mortgages is paid monthly to the investors holding certificates backed by the loans securitized. In this method of selling loans, FDIC and RTC set up two types of funds - the Credit Enhancement Reserve Fund and the Payment Retention Fund—for each securitization transaction. Credit enhancement reserve funds are established to achieve the desired credit rating for the securities issued and to make up losses to investors resulting from defaults of securitized loans. Credit enhancement reserve funds are managed by trustees with the help of loan servicers. Payment retention funds provide the master servicer with funds to make up for any shortfall in loan payments during the transfer of servicing from the pre-securitization servicers. Any balance from the payment retention funds, when all the loans are securitized, should now be returned to FDIC.

During the reporting period, the OIG completed an audit of the RTC's two credit enhancement reserve funds for mortgage pass-through certificate series 1992-07. The OIG's objectives in looking at these reserve funds were to determine whether (1) non-performing loans were adequately serviced; (2) withdrawals from the reserve funds were allowable, supported, and correctly calculated; and (3) the trustee invested credit enhancement reserve funds in permitted securities.

The servicing of delinquent loans for Securitization 1992-07 was adequate. Generally, Chase, the securitization's servicer at the time of our review, took steps to obtain late payments, bring borrowers current, obtain property inspection reports, and initiate foreclosure proceedings in a timely manner. Chase used an automated telephone calling system to contact delinquent borrowers and followed these calls with computer-generated collection letters. This capability allowed Chase to effectively and timely monitor and collect or foreclose on delinquent loans.

However, American Residential Mortgage Corporation (the original servicer) and Chase claimed \$255,736 for loan losses that they could not adequately support. The servicers advanced funds to cover principal and interest payments and certain property expenses for defaulted loans. When loan losses occurred, the losses were reimbursed from the two credit enhancement reserve funds or the securitization's excess cash pools. However, Chase could not always provide documentation explaining how the servicers calculated their loan losses.

In addition, MGIC Investor Services Corporation, whose role it was to determine whether losses reported on officers' certificates resulted from breaches of representations and warranties, did not review five liquidated loans for such breaches. Chase was not able to supply the necessary documentation for MGIC to conduct its review. Because Chase could not produce the loan files for these five loans, \$262,155 in loan losses reimbursed to American Residential and Chase could not be validated.

When we presented our report to the Audit Committee, members expressed concern that there could be potentially higher questioned costs than what the audit had revealed. The Committee requested Office of Internal Control Management (OICM) representatives to review the specific conditions raised in the audit, consider their broader implications for the Corporation, and report back to the Committee.

Division of Resolutions and Receiver-ships (DRR) staff acknowledged that the former servicer had been problematic and that problems were exacerbated when the new servicer underwent a corporate merger. DRR also indicated that staff would take steps to more strongly emphasize to servicers their obligations under servicing agreements and that DRR would expand its oversight and procedures reviews.

---

**Property Tax Reassessment and Tax Refunds Work Questions  
\$4.5 Million**

By way of background, RTC OIG's audit report, *Property Tax Reassessment and Tax Refunds*, issued on December 14, 1995, found that RTC's California Office could not confirm that it had received \$3 million in tax refunds on successful tax appeals initiated by subcontractors of expired RTC Standard Asset Management and Disposition Agreement (SAMDA) contractors and did not have a complete list of about \$1.4 million of appeals in progress.

The Vice President of the California Office responded to the report recommendations by forming a task force to trace and identify commission payments on finalized appeals to determine if RTC had received the refunds. He also reiterated that the California Office had engaged a tax appeal contractor to track and collect refunds due from county property tax authorities. The contractor was providing monthly and/or quarterly reports to which RTC could reconcile its own records of outstanding appeals and refunds.

When RTC was dissolved December 31, 1995, the task force was disbanded and responsibility for resolving outstanding issues of expired SAMDA contracts was shifted to Division of Administration (DOA) Contracts in FDIC headquarters, possibly including much of the \$3 million and \$1.4 million of appeals and refunds which could not be accounted for by the California RTC Office.

FDIC's policies and procedures emphasize the importance of reviewing assessments and initiating challenges, when appropriate, for assets owned by the FDIC as receiver or in its corporate capacity. During this reporting period, FDIC's OIG conducted an audit that reviewed all Western Service Center (WSC) unsold properties held in receivership to determine whether appeals were filed for properties meeting the appropriate criteria. Several weaknesses were found, as described below.

Our review found that WSC's efforts were insufficient to recover previous payments of property tax penalties and special assessment fees related to FDIC-owned real estate from which the FDIC was exempt. As a result, payments of \$3.5 million in tax penalties and \$854,674 in special assessments were not recovered from various California county tax authorities. In addition, the WSC did not always request the tax appeal contractor to appeal excessive property tax assessments. As a result, potential property tax refunds of \$64,195 in 1995 and \$54,941 in 1994 were not obtained.

Further, WSC's management of property tax assessment appeals and resulting refunds was not adequate to ensure that refunds were reimbursed to the FDIC funds in a timely manner. In addition, WSC did not always record appeal refunds when received and credit the appropriate general ledger accounts. WSC also paid some commissions to the tax appeal contractor although no refunds were received. Additionally, FDIC did not adequately identify and recover refunds from successful RTC property tax appeals initiated by subcontractors of expired SAMDA contractors. Finally, WSC did not pay its contractor, Property Research Limited, Inc., timely.

Although our audit focused on property tax issues in the WSC, the OIG believes the problems identified may exist at other FDIC locations. We brought this point to the Audit Committee's attention at one of its monthly meetings. In response, the Committee requested OICM, in cooperation with DRR and Division of Finance (DOF) to determine whether similar lapses in internal controls exist elsewhere; to address the issues identified in our report; and to initiate procedures to ensure that similar lapses in oversight control do not occur in the future.



---

## **Supervisory and Regulatory Activities Are Key to FDIC's Success**

FDIC's supervisory and regulatory responsibility is designed to ensure the safety and soundness of federally insured depository institutions. FDIC is the primary federal regulator for over 6,200 state-chartered banks whose deposits are covered by FDIC insurance funds. The Corporation also has certain backup supervisory authority, for safety and soundness purposes, for savings institutions, national banks, and state-chartered banks that are members of the Federal Reserve System. With the increased financial strength of the banking industry, the number of failed banks continues to decrease. During calendar year 1996 and the first 9 months of 1997, 6 banks have failed, compared to 19 banks that failed during 1994-1995. In the years 1992-1993, 161 banks failed. With the increased vitality of the banking industry and the continued trend of mergers resulting in larger, more complex institutions, FDIC's primary focus has turned to identifying and addressing the potential risks to the banking industry and deposit insurance funds rather than on resolving failed institutions. FDIC's challenge continues to be to maintain the viability of the federal deposit insurance funds. To meet the challenge, FDIC must identify and take action on any institution whose practices are unsafe, unsound, illegal, or improper before the practices result in a drain on the insurance funds.

In recent testimony on the Future of Bank Examination and Supervision before a House Subcommittee, Acting Chairman Hove stated that FDIC is engaging in more proactive and risk-focused strategies as a framework for future supervision. Management is concentrating its resources on external factors—macro and regional economic trends that can affect many banks. It is also focusing examinations on the bank's ability to manage its risks. In addition, the FDIC is gathering and analyzing more information off-site, although the Corporation has learned through experience that there is no substitute for regular on-site examinations of depository institutions. Finally, management has engaged in a continuous process of reviewing its regulations to reduce unnecessary regulatory burden.

The FDIC has taken a number of important steps as it looks to the future. One of its recent refinements to the bank examination process is a joint initiative with the Federal Reserve Board that provides a more structured and risk-focused approach towards supervision. The objective of this initiative, which was recently implemented, is to evaluate more effectively the safety and soundness of a bank by focusing examination resources on a bank's greatest risk. This structured risk assessment approach allows examiners to look beyond the static condition of a bank to how well a bank can respond to changing market conditions given its particular risk profile.

Acting Chairman Hove also has stated that more than ever, the pivotal factor in determining the appropriate scope for an examination is the accurate assessment of bank management's ability to identify, measure, monitor and control risks. Thus, FDIC management is seeking more effective ways to address emerging risks in institutions before

those risks develop into serious problems. In this regard, the FDIC has also initiated efforts to identify and address negative trends arising in the credit card industry, subprime lending, personal bankruptcies, and syndicated loans areas.

The banking industry has moved into such new services as cyberbanking, smart cards, and other highly technical financial delivery systems. It is vulnerable to new types of electronic fraud. It is also susceptible to regional and economic sector fluctuations in the economy. As such, there is continuing interest in legislative changes affecting the banking industry, such as merging the bank and thrift charters. The Congress and public look to the FDIC to manage these challenges in a manner that ensures the safety and soundness of banking institutions and the preservation of the insurance funds that back insured depositors.

---

### **Audit of the Oversight of Newly Chartered Institutions by the Division of Supervision's Atlanta Regional Office**

In 1995, the OIG reviewed a trend among bank failures that newly chartered institutions appeared to have a higher failure rate than institutions with more operating experience. The increased risk associated with newly chartered institutions highlighted the need for the FDIC to ensure that applications for federal deposit insurance are properly evaluated and that these newly chartered institutions receive effective supervisory oversight.

We recently conducted an audit of the oversight of newly chartered institutions by the Division of Supervision's (DOS) Atlanta Regional Office. We concluded that Atlanta had performed comprehensive reviews of applications for federal deposit insurance and consistently evaluated the seven statutory factors provided in Section 6 of the Federal Deposit Insurance Act (FDI Act). Atlanta's application reviews were not only comprehensive, they were also timely, with most applications processed within 120 days. Our audit identified five opportunities where the application process could be improved to further minimize risks to the deposit insurance fund. The areas of improvement include: (1) additional methods to identify underlying weaknesses related to proposed directors and officers, (2) early development of policies and controls in newly chartered institutions to improve performance during the first 3 critical years of operation, (3) application files that provide a complete history of events and decisions that occur during the application process, (4) examination reports that include an analysis of any significant departures from initial projections, and (5) examinations that are conducted in compliance with FDIC's examination frequency policy and statutory requirements. FDIC management officials agreed with each area identified during the audit. They have indicated that corrective actions have been or will be implemented.

---

#### **Material Loss Review- The Failure of First Trust Bank, Ontario, California**

In accordance with Section 38(k) of the FDI Act, the OIG conducted a material loss review of the failure of First Trust Bank, Ontario, California. This bank closed in 1995, with total assets of \$245.6 million. It was estimated that the Bank Insurance Fund would be subject to a loss of \$16.1 million as a result of the closure. However, in 1996, FDIC's DOF revised the estimated loss. DOF officials notified the OIG that, as a result of subsequent accounting adjustments for liquidation activity, the Bank Insurance Fund would incur a loss of \$34.5 million, an amount that would trigger the requirement for a material loss review.

Three primary reasons for the failure of First Trust were identified — changes in management's business philosophy, concentrations of direct real estate investments, and concentrations of construction and development loans. These conditions were exacerbated by a local economy that experienced a severe downturn in the early 1990s.

By law, the OIG is also required to comment on the adequacy of DOS' regulatory oversight of failed institutions meeting the requirements for a material loss review. For First Trust, we concluded that the bank's significant problems were identified and addressed by examiners and that DOS complied with the requirements of Section 38 of the FDI Act, Prompt Corrective Action. However, we observed that DOS's supervision of First Trust could

have been strengthened in the following areas: (1) the timeliness and effectiveness of supervisory actions, (2) the examination frequency of the bank, (3) the rating of asset quality, and (4) the experience level of the examination teams. Management officials expressed agreement with this report and indicated that they planned to implement corrective action.

---

#### **Allegations Regarding Disclosure of Confidential LippoBank Information**

The FDIC's report of examination is highly confidential. Although a copy is provided to the bank, that copy remains the property of the Corporation. Without FDIC's prior authorization, directors, officers, employees and agents of a bank are not permitted to disclose the contents of a report. Further, federal statutes prohibit federal employees from disclosing information about the operations of an organization and examiners from disclosing the name of any borrower or description of collateral for a loan gained during the course of an examination. Early in this reporting period, the OIG was asked to review how well the Corporation had followed its policy and the statutes in handling issues surrounding LippoBank in Los Angeles, California.

Media and congressional interest had focused on LippoBank and its relationship with FDIC in light of contributions to the Democratic National Committee made by an associated Indonesian federation of companies — LippoGroup. Further, the relationship between the Riady family, the owners of the LippoGroup, and President Clinton, had been scrutinized by the Congress and the media. In one particular article

appearing in the November 14, 1996, *Business Week*, confidential FDIC information on LippoBank was disclosed, namely its preliminary 1996 examination results.

On November 27, 1996, the President and Chief Executive Officer of LippoBank sent a letter to FDIC alleging that the FDIC disclosed confidential information to the press. We reviewed the allegations at the request of FDIC's Vice Chairman to determine whether (1) criminal misconduct on the part of FDIC employees had occurred in the handling of confidential LippoBank information, (2) FDIC adhered to its policies and procedures and exercised due professional care when providing LippoBank information to others, and (3) adequate controls existed to prevent unauthorized disclosure of confidential LippoBank information.

Our evaluation did not reveal the source of the disclosure, but it confirmed that confidential information had been disclosed to the press. Around the time of the disclosure, FDIC and the California State Banking Department had been examining LippoBank, and outside parties, including staff from various Congressional committees and the Board of Governors of the Federal Reserve System, had been reviewing confidential FDIC information on LippoBank.

All FDIC employees, including examiners assigned to the current LippoBank examination, and California State Banking Department examiners, denied speaking with the media or disclosing confidential LippoBank information.

Further, our Office of Investigations did not identify any information or evidence that FDIC may have been involved in improperly providing information to the press. Still, to avoid future disclosures of confidential information, we recommended improved security procedures.

In response to our recommendations, management indicated that it intended to prepare a resource guide based on its "Best Practices" review. The resource guide will memorialize key practices, procedures, issues and legal research regarding Congressional document productions for the benefit of future efforts. In addition, management planned to reinforce the expectation of secure storage of confidential supervisory records by upgrading security at the East Los Angeles Field Office. Finally, DOS indicated it would conduct an evaluation to determine whether its guidelines for handling confidential records were sufficient and develop training programs or other communication vehicles on managing confidential records.

---

### **Corporation Must Carefully Evaluate Future Information Technology Needs**

---

FDIC's strategic plan emphasizes the Corporation's commitment to enhance its use of technology to accomplish its mission and strategic goals. Corporate initiatives in this area seek to identify, develop, and implement new information technologies that will improve the effectiveness and efficiency of all aspects of the Corporation's primary activities in its supervision, insurance, and policy, regulation, and outreach programs. FDIC managers need reliable information from a multitude of systems on which to base important business decisions in their areas of responsibility. The Corporation budgeted \$233 million in 1997 to be used by Division of Information Resources Management (DIRM) as the lead organization for FDIC's information resources management activities. As for 1998, approximately \$217.5 million was being considered as a budget.

Two goals related to the technological resources function are articulated in the Corporation's strategic plan. The first goal is to ensure that all corporate automated systems are Year 2000 ready. That is, computer software must be able to distinguish between the year 2000 and 1900. The risk exists that computers may fail at the turn of the century in one of three ways: they will reject legitimate entries, or they will compute erroneous results, or they will simply not run. In fulfilling the goal of Year 2000 readiness, staff will need to assess, renovate, test, and implement computer application systems that are Year 2000 compliant. Staff will also need

to assess, test, and replace as necessary any telephone network, or computer hardware that is not Year 2000 compliant. As a second goal, the Corporation will identify, evaluate, and implement new systems and technological approaches for meeting corporate strategic goals. In this regard, the Corporation has stressed the importance of obtaining broad-based input that encourages innovation and particular attention to user input as services and systems are developed.

The OIG's work in the information resources area is designed to determine whether FDIC is effectively managing its information resources management program and economically meeting the financial management and information needs of its corporate users. The OIG looks at systems already in place as well as at systems under development. Another important realm of OIG activity is in the systems security area. That is, OIG work also addresses the controls in place to ensure the integrity and security of the Corporation's technological resources.

Several audits and related projects from the current reporting period illustrate the OIG's attention to the Corporation's technological resources function.

---

### **Progress on Y2K Project**

During the past 6-month period we reported on ongoing work related to the Year 2000 (Y2K) project. We completed our review of the Corporation's awareness phase of the Y2K Project and determined that the Y2K program office has adequately defined and explained the importance of achieving Year 2000 compliance on a corporate-wide basis. We issued a memorandum to the Director of DIRM summarizing the results of our review. We acknowledged that the project had been

well documented, as evidenced by updates to the Information Technology plan that reflected the current status of the project. In addition, DIRM established the Y2K project team. This team had defined compliance and standards, assigned roles and responsibilities, and essentially completed collecting system application inventory data.

Our overall audit objectives as we continue our work are to determine whether (1) the development will adhere to the structured approach and the rigorous program management that is needed to decrease risk, (2) user needs have been adequately defined, and (3) systems deliverables will satisfy user needs in a cost-effective and timely manner. The project team will conduct the Y2K analysis in five phases—awareness, assessment, renovation, validation, and implementation.

---

### **GENESYS Development**

One of the Corporation's most important systems initiatives is development of an automated examination package called GENESYS. GENESYS will provide automated support for all functions required to perform an FDIC safety and soundness examination and report. The system will be installed on examiners' laptop computers and will facilitate electronic capture of data pertinent to the examination, provide analysis capabilities, and provide Report of Examination generation capabilities to facilitate production and delivery of examination reports. The Corporation expects to have GENESYS completed and ready for use in the fourth quarter of 1998.

We conducted a review of GENESYS and identified opportunities for improving the system development practices related to the project. Senior management was generally aware of the project's scope and objectives. However, the GENESYS project team had not completed a feasibility study or finalized a cost-benefit analysis for GENESYS. Although the GENESYS project team had developed several draft versions of a project work plan describing the scope, resources, and time schedules necessary for developing the system, it had not obtained senior management approval. In addition, user requirements had not been completely defined by the project team or approved by senior management. Although a cost-benefit analysis, project work plan, and functional requirements document had not been finalized or approved by senior management, detailed design and development work had been initiated for some portions of the project. We also noted that a quality assurance specialist had not been assigned to the project to ensure adherence to system development life cycle (SDLC) procedures.

Performing detailed design and development work before previous SDLC phases and key deliverable products have been finalized and formally approved by senior management presents unnecessary risk to GENESYS' being implemented in the most timely and cost-effective manner.



In addition, although GENESYS design and development work had been initiated, DIRM had not determined the impact that GENESYS and other planned development projects would have on FDIC's data communications networks located in the 98 DOS field offices. Network connections between the 98 DOS field offices and the Wide Area Network have significantly less capacity than connections between FDIC's mainframe and headquarters offices, service centers, and regional offices. We pointed out that evaluating the adequacy of FDIC's existing data communications networks should be addressed as part of the GENESYS requirements analysis. We made recommendations to management to address problems noted. In response, management agreed to take actions to address all of our concerns.

---

#### **TAPS and ETVS**

Two additional systems development efforts received audit attention during the past reporting period. The Corporation's Time and Attendance Processing System (TAPS) and its Electronic Travel Voucher (ETV) System are initiatives that are intended to facilitate the often cumbersome administrative processes related to travel and time keeping.

The TAPS development effort is a major initiative intended to re-engineer FDIC's time and attendance process. It will also be one of the initial systems at FDIC to employ digital signature technology for certifying and approving records. The significance of the development effort coupled with the implementation of new technology warrants close audit involvement.

The OIG's review of TAPS raised several issues. Although work had been performed on a number of SDLC phases, the TAPS project team did not (1) finalize critical SDLC deliverables such as an analysis of alternatives and a cost-benefit study and receive senior management approval before proceeding with the subsequent phases; (2) revisit costs and benefits when significant changes occurred in the project scope, cost, and schedule; (3) provide senior management with the detailed information needed to monitor the TAPS development effort; and (4) finalize and receive approval for TAPS requirements before initiating external and internal design work. These deviations from accepted practices put the project at risk and resulted in additional effort and cost. The TAPS project manager estimated that as much as 85 to 90 percent of design work would have to be re-performed, with additional costs of \$1.9 million.

The OIG recommended that critical early stages of the SDLC process be completed and approved by FDIC senior management before initiating substantial amounts of work on later stages of the SDLC process. We also recommended that the project team prepare progress reports and minimize or eliminate overlap of SDLC phases.

In a similar vein, we advised the Directors of DIRM and DOF via memorandum that our review of the external design phase of the ETV project determined that the project was following generally accepted system development procedures. The work was well planned, as evidenced by updates to the project plan reflecting its status. As the project team completed the planning and requirements phases of the project, the work plan was updated.

Completion dates for various tasks were extended but the implementation date of November 3, 1997 remained constant. We expressed concern that if the project continued to be driven by the original target date for implementation, all of the procedures required by the SDLC manual may not be successfully completed and the quality of the system may not meet the original standards.

---

#### **OIG Examines System Security Issues**

Two additional audits in the information resources area addressed security issues. The OIG conducted audits of two of the Corporation's main operating systems - Customer Information and Control System (CICS) for the IBM and Amdahl Mainframe Computers and the UNIX/Oracle Software residing on a Sun midrange computer. These operating systems are highly complex and support a number of significant corporate applications. It is important that the integrity of these systems be maintained and safeguarded against security breaches.

Particularly in an environment of downsizing, the Corporation must guard against disgruntled employees who may wish to strike out against the Corporation. The Corporation must ensure that its powerful operating systems are not vulnerable to tampering or other unauthorized manipulation. The consequences of security weaknesses could range from disclosure or modification of sensitive information to a complete disabling of the Corporation's business operations and result in millions of dollars in losses.

CICS, is a secondary operating system that provides the interface between on-line applications systems and the computer's operating system. One of its main functions is, upon a user's command, to call the appropriate computer program, pass the user's data to that program, and then pass the response from the program back to the user. CICS resides on both of the Corporation's mainframes. The existence of two mainframe computers, the IBM and the Amdahl, resulted from FDIC's acquisition of the IBM unit from RTC in the course of the merger of the two Corporations.

Among security weaknesses found in the IBM environment were system start-up procedures which could potentially weaken overall security protection. On the Amdahl mainframe, we found inadequate safeguards over the storage area used to house powerful computer programs capable of by-passing the security facilities. On both mainframes we found a number of instances in which an excessive number of system users had access to powerful CICS commands which could disrupt computer services. Finally we found a number of fundamental differences existed in implementation parameters and options between the two mainframe computers which could hamper future consolidation into a single mainframe.

The UNIX/Oracle server houses approximately 20 applications systems, several of which serve critical functions such as the tracking and management of information relevant to bank resolutions, assistance agreements, staffing, operations planning, and employee buyouts. In addition, several mainframe-based systems interface with the server for reporting purposes. With respect to UNIX, we found that password management needed to be improved and that access to sensitive files was not sufficiently restricted. We identified several thousand files that could be read, modified, or deleted by any UNIX user and almost as many programs that could be executed by any UNIX user. Among the security weaknesses found in the Oracle environment were broad system privileges inappropriately assigned to Oracle users that could severely impact security, operational efficiencies, and maintenance activities.

---

### **Difficult Personnel and Downsizing Issues Must Be Addressed**

---

In the aftermath of the banking crisis of the late 1980's and early 1990's, FDIC staffing peaked in mid-1993 at 15,611. Since that time, FDIC has significantly reduced the size of its workforce to 8,044 as of September 30, 1997. The degree of downsizing at FDIC is largely unprecedented in government. This fact becomes even more apparent when one takes into account the inherited workforce of RTC. At the time of RTC's merger with FDIC at the end of December 1995, the Corporation inherited approximately 2,000 people from RTC.

Over the past several years as the health of the banking industry has improved significantly, the work associated with resolving institutions and liquidating assets has sharply declined. In late 1995, FDIC initiated a successful buyout program that resulted in the voluntary separation of about 900 permanent employees. In 1996, the Corporation formulated a comprehensive strategy for further staffing reductions over a 3-year period from 1997-1999. This downsizing program involved a second buyout, targeted to areas of excess staffing, that resulted in 400 more voluntary departures of permanent staff; the phased consolidation of six existing field liquidation offices to a single site, with corresponding staffing reductions; an extensive out placement effort; cross-training of over 200 permanent employees to fill bank examiner and other vacancies within the Corporation; and reductions-in-force.

It was anticipated that these initiatives would result in a reduction of FDIC staff from about 11,850 employees at the beginning of 1996, after the integration of RTC operations and staff, to between 6,500 and 6,600 by year-end 2000. Such a shift would also complete the transformation of the Corporation to an organization focused on anticipating problems rather than one that responds to problems within the industry.

Generally, FDIC's downsizing and restructuring actions have thus far been reasonable and well planned. However, challenges persist. The Corporation must make sure it matches workload and staffing in a way that is equitable and efficient. With offices closing or consolidating, major transfers of functions, resources, information, and knowledge occur that may be disruptive to the conduct of critical business. There are significant costs associated with reducing or moving staff, closing offices, and building out space. Decision makers must carefully consider such issues as the most economical actions to take, the timing of office closures, and availability of knowledgeable staff for critical assignments and potential crises.

---

#### **OIG Reviews Key Downsizing Concerns - Staffing and Space**

Given the magnitude of FDIC's downsizing efforts, it is not surprising that staff members themselves would feel somewhat anxious and threatened with respect to their livelihoods. We conducted an evaluation review in response to an inquiry made by Senator Paul Sarbanes who had received an anonymous letter from a group of permanent FDIC employees alleging that DOA's Acquisition Services Branch (ASB) (1) extended five of its

employees' term appointments beyond December 31, 1995, which in several cases exceeded the United States Office of Personnel Management 4-year limitation; (2) converted these employees' term appointments to permanent positions by announcing positions considering status and non-status candidates while concurrently preparing to conduct a reduction-in-force; and (3) improperly employed a student who was on a term appointment with full benefits for an excessive time frame.

The results of our review showed that DOA's ASB and Personnel Services Branch followed applicable policies and guidelines in extending the term appointments of the five employees mentioned in the allegation. We also determined that only one of the five employees' term appointments was converted to a permanent position and that the conversion and accompanying promotion were performed and approved in accordance with prescribed policies and guidelines. However, we identified several issues related to the term extensions and conversions that warranted FDIC's attention.

In response to our report, DOA (1) posted on the Corporate Issues Bulletin Board an explanation of the application screening process used by the Personnel Services Branch for determining preferential reassignment eligibles, (2) issued guidance to ensure that conversions are justified and consistent with core staffing, and (3) agreed to periodically monitor the extent of conversions by division and establish a minimum time period under which employees hired or converted to permanent status would be excluded from any future buyout offers.

Downsizing often entails consolidating office space and/or renovating existing corporate locations to accommodate shifts in staffing and work assignments. FDIC has faced such demands over the past several years. To illustrate, in April 1996, the Corporate Services Branch recommended to the Administrative Committee that it was necessary to renovate Virginia Square to accommodate the consolidation of RTC and FDIC staff and other construction resulting from the Corporation's overall downsizing. This project was placed on a "fast track" because personnel in buildings with expiring leases needed to vacate those buildings by October 1996.

The OIG conducted an evaluation to determine whether (1) FDIC effectively planned and managed the contract for the General Contractor that provided tenant improvement services at Virginia Square and (2) the remodeling and improvements were necessary and within Corporate standards.

Our evaluation showed that the actual cost of the General Construction Contractor exceeded the original amount authorized because the original amount was based on a preliminary set of drawings and additional work requirements were added after the contract was approved. These additional work requirements and their associated costs were justified in an October 29, 1996, request for additional expenditure approval submitted to the Deputy to the Chairman and Chief Operating Officer (COO).

### **OIG Plays Greater Role in the Audit of FDIC's Financial Statements**

The Chief Financial Officers Act requires that government corporations have their financial statements audited annually and that such corporations submit an annual management report to the Congress. The U.S. General Accounting Office (GAO) has in the past been primarily responsible for the audit of FDIC's financial statements, and the OIG has provided support by conducting separate audits that GAO could rely upon to render opinions on the statements. These roles, however, are shifting, and GAO and the OIG are working together with the ultimate goal of the OIG assuming full responsibility for the audit.

The OIG's increased involvement with the annual audit began in 1995. For the calendar year 1996 audit, the OIG dedicated senior level audit specialists as replacements for GAO managers. During this past reporting period, while still under GAO's direction, the OIG has been more involved in planning and coordinating the audit. During the coming year, GAO will be removing some of its staff from the assignment, while the OIG will be assigning even more of its staff to the effort.

The OIG has assured GAO management of the commitment to this project and the long-term importance of the FDIC financial statement audit to the OIG. The transition and the audit project are progressing well, and the OIG and GAO management have agreed that there are mutual benefits of the ultimate OIG takeover of the annual financial statement audit. GAO welcomes the reassignment of some of its staff to other GAO activities at a time when GAO is dealing with budgetary cutbacks and an overall reduction in staff. The OIG expects the Corporation to benefit through OIG efforts to streamline the audit process and provide cost savings to the Corporation.

The original approved procurement requisition authorized \$1.8 million in expenditures. The COO approved the October 29, 1996, request and a procurement requisition adding \$973,439 in expenditure authority was executed to reflect the additional work. This requisition increased the total expenditure authority for the contract to a total of \$2.8 million.

We found no instances in which the remodeling and improvements were above corporate standards. Following receipt of the General Construction Contractor's bill for services, DOA did take steps to ensure the Corporation received those services at fair and reasonable prices. However, as acknowledged by DOA management in the request for expenditure approval, the monitoring and administration of the contract could have been better.

We also determined that in addition to the primary contract, the Corporation incurred almost \$1.5 million in other contractor costs directly related to the renovation project, bringing the total cost to renovate and update the office building at Virginia Square to about \$4.3 million. These additional contracts were not part of the DOA budget for Buildings and Improvements. Rather, the contracts were either budgeted for in other DOA line items or were part of DIRM's budget. DOA did not inform senior management of the totality of contracts and costs involved in the project. In the case of Virginia Square, these additional costs were 52 percent of the construction costs. DOA officials explained that DOA has consistently used only the construction costs in computing the cost of renovations.



We did not make formal recommendations to management. However, we suggested that if other contract costs, such as those for furniture, fixtures, equipment, cabling, and carpet, are usually a significant percentage of the construction contract for a renovation project — as was the case at Virginia Square — DOA should consider including those costs in reporting renovation costs. We believe that such information would be useful to senior management for decision-making; in particular, for approving office moves and renovations.

Management agreed that for future renovation projects, once the scope of work is well defined and detailed plans are established, it would develop cost estimates that consider all costs associated with the projects and submit that information to senior management for its consideration in approving such projects. Management also agreed to track and report all costs of the projects as they are completed to help ensure that the Corporation's actual total costs for projects are within the total estimated cost.



Summer interns assisted OIG staff during the past reporting period in work related to major issues facing the Corporation. Pictured here with the Inspector General: Front row l to r: Latina Wilson, Holly Meeuwissen, Sherrell Thompson. Back row l to r: Jeffrey Sears, Brian McDowell, John Sakhleh, Gaston Gianni. Not pictured: Jim Moye.

## Investigations

Contractor Cases

Fraud Impacting Financial Institutions

“Con-schemes”

Employee Cases

The Office of Investigations is responsible for investigating fraud and other criminal activities impacting FDIC and its programs. Although our primary focus is on detecting and investigating criminal misconduct, we also are called upon to investigate violations of FDIC rules and regulations when the alleged violation is serious enough and/or the potential consequences to the FDIC grave enough to warrant such attention. During the last 6 months, the Office of Investigations opened 53 and closed 73 cases. At the end of the period, we had 177 cases in progress.

Indictments or criminal charges were brought against 16 defendants this period. Our cases also resulted in the conviction of 9 individuals. Fines, restitution and monetary recoveries resulting from our cases this period totaled over \$4.6 million. Our efforts also led U.S. Attorney’s Offices to file civil suits against 12 defendants this period seeking over \$9 million in damages as a result of their alleged fraudulent acts.

As illustrated in the cases highlighted for the period, our investigations arise from a variety of sources and may focus on an array of fraudulent schemes. Our results this period reflect the considerable efforts we have historically devoted to investigating alleged abuses by contractors. In addition to traditional investigative approaches in this area, we have worked closely with FDIC officials in proactive initiatives designed

### Investigative Statistics

#### Judicial Actions:

Arrests	2
Indictments/Informations	16
Convictions	9

#### Actions Involving FDIC Employees as a Result of Investigations:

Removals	1
Suspensions	1

#### OIG Investigations Resulted in:

Fines of	\$ 268,500
Restitution of	\$3,183,994
Monetary Recoveries of	\$1,150,316

#### Cases Referred to the Department of Justice (U.S. Attorney)

19

#### Other Referrals:

FDIC Management	8
State/Local	1

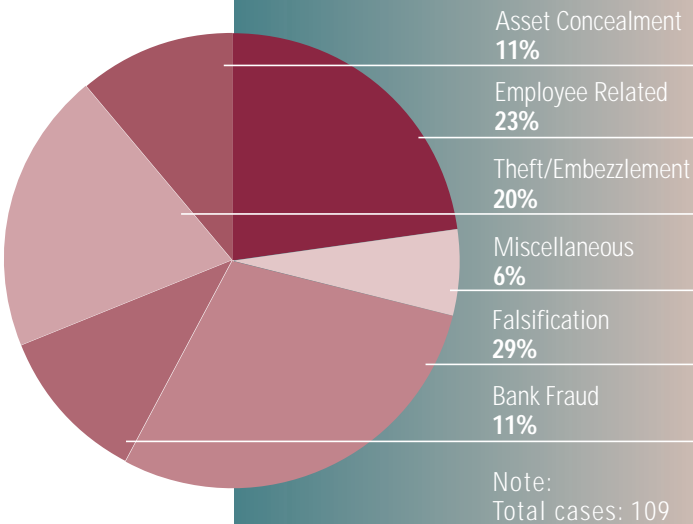
#### OIG Cases Conducted Jointly with Other Agencies

29

to identify contractors of the former Resolution Trust Corporation (RTC) who are holding funds now due FDIC. In light of the voluminous number of contracts RTC had with property managers, loan servicers, and outside counsel, the existence of such funds was at risk of going undetected when RTC went out of business. Our work with FDIC in this area has already led to the identification and collection of substantial sums of money due from former RTC contractors. It has also led to the successful criminal prosecution of one contractor.

Our past emphasis on fraud cases arising at FDIC or former RTC-controlled institutions is also reflected in the results we are reporting this period. Other cases highlighted for the period involve fraudulent schemes by individuals falsely claiming to be representing the FDIC, as well as criminal misconduct by FDIC employees.

Figure 1: Fiscal Year 1997  
FDIC OIG Investigations by Type





## Contractor Cases

The FDIC OIG continues to devote resources to detecting and investigating fraudulent activities of contractors. Several of our cases in this area met with significant results this period. Earlier we discussed coordinated efforts that led to the guilty plea of a New York attorney to charges that he defrauded the FDIC and RTC and obstructed an OIG audit. (See discussion of criminal case in Major Issues section.)

A 2-year investigation of another contractor culminated this period in the indictment of an Ohio Corporation, one of its senior officers, and two former senior officers, on charges of wire fraud, false claims, conspiracy, and impeding the functions of RTC. The corporation, a wholly owned subsidiary of a publicly traded national corporation, is engaged in a number of business operations, including loan servicing.

The corporation was among a number of contractors responsible for servicing residential mortgage loans that the former RTC had acquired from failed savings and loans. The RTC sold these loans by assembling them into large bundles and offering them to the public as "mortgage-backed securities." The securities were underwritten and marketed by Wall Street brokerage firms. The RTC was responsible for ensuring the continued servicing of the individual residential mortgage loans, including the collection, payment, and record-keeping functions associated with each loan. The Ohio corporation served as the master servicer on nine series of these mortgage backed securities and, in that capacity, was responsible for servicing thousands of loans included in each series.



The indictment alleges that the corporation and the three other defendants provided incorrect and incomplete information to the RTC when RTC attempted to reconcile amounts due from the servicing of the loans. The defendants allegedly engaged in a scheme to obtain over \$3.5 million from the RTC, knowing such funds were not due them. Additionally, the three senior corporation officials allegedly instructed other employees of the company not to disclose to the RTC the true amount of funds collected.

As a result of another contractor investigation, conducted jointly with the FBI, two Oklahoma men were indicted on charges of conspiracy, mail fraud, wire fraud and money laundering. The men were employed by a Tulsa firm that had contracted with the RTC to collect on defaulted loans that RTC had acquired from various failed savings and loans. In addition to debt collection, the firm was authorized to negotiate settlements with the RTC debtors. Under the contract, the firm received a portion of funds it collected on behalf of RTC.

As outlined in the indictment, the men, who had been assigned to handle the RTC work for the firm, allegedly embezzled almost \$139,000 in funds that the firm was to have collected on behalf of RTC. The men allegedly did so by depositing funds they had collected from RTC debtors into a bank account they controlled. In some instances, they arranged for the debtors to wire transfer their settlement

payments directly to the account. In carrying out the scheme, the two made overly generous settlement offers to some debtors. For instance, they negotiated a \$15,000 settlement on a judgment of nearly \$2 million owed RTC. They also forgave another \$2 million debt for a settlement of \$85,000. In each instance, the men pocketed the entire amount of the settlement funds.

As a result of another case involving servicing of RTC debts, an employee of a former RTC contractor was sentenced to serve 12 month's confinement in a halfway house, followed by 48 month's probation, and was ordered to pay \$208,771 in restitution to FDIC, after pleading guilty to conspiracy charges. A financial consultant who conspired with the contractor employee to defraud the former RTC also pleaded guilty to conspiracy and was sentenced to serve 6 month's home detention, 48 month's probation, and was ordered to pay restitution of \$10,000.

Our investigation of the two individuals was initiated based upon information provided by a Florida firm that served as a loan servicer for the RTC. The firm notified the RTC when it became suspicious of the activities of one of its employees who had been assigned to handle loan work-outs of RTC debts. The resulting investigation found that the contractor employee provided confidential information regarding RTC loans to the financial consultant. The consultant then contacted the debtors on those loans and offered, for a fee, to negotiate discounted settlements of the loans. In exchange for half of the fees collected by the consultant, the contractor employee arranged for the loan reductions.

Our investigation determined that the contractor employee discounted 84 different loans in this manner, with total reductions in funds of over \$1.4 million. The consultant fraudulently collected approximately \$400,000 in fees from the RTC debtors, and paid the contractor employee \$200,000 in illegal kickbacks for his role in obtaining the discounted settlements.

One of our successful contractor investigations this period was initiated based upon information developed during a review by the OIG's Office of Quality Assurance and Oversight. That investigation, conducted jointly with the U.S. Secret Service, focused on a Massachusetts man whose company subcontracted to manage properties that the RTC had acquired from various failed savings and loans in New England. Following our investigation, the man pleaded guilty to a criminal information charging him with embezzlement and receiving a kickback. He was subsequently sentenced to serve 5 months of home detention, followed by 3 year's probation. He was also fined \$61,000 and ordered to pay restitution of \$31,050 to FDIC.

The investigation found that the property manager embezzled over \$200,000 from the operating accounts for the properties, sometimes charging for work that was not performed, other times taking funds directly from the accounts. The property manager also accepted a \$1,000 kickback directly from a demolition subcontractor he had recommended for an RTC job.

---

In addition to criminal prosecutions resulting from our contractor investigations, one of our cases this period led the U.S. Attorney's Office for the Central District of California to file a lawsuit seeking multi-million dollar damages from three individuals under the False Claims Act. The civil complaint alleges that the defendants fraudulently obtained contracts from the FDIC and the former RTC and overbilled both agencies. Among the defendants named in the suit is a California businessman who owns one of the largest auction companies in the nation. The auctioneer's wife and the wife's brother-in-law, a certified public accountant, are the other defendants.

The lawsuit alleges that in order to obtain lucrative contracts under the FDIC and RTC Minority- and Women-Owned Business programs, the couple falsely certified to the two corporations that a company established by the husband was owned and controlled by the wife. The company was actually a "shell" for the husband's huge auction company. Based on these alleged false representations, the shell firm was awarded contracts to perform more than a dozen auctions on behalf of the FDIC and RTC. These auctions, held in California, Texas, Louisiana, Massachusetts, Connecticut, and New Jersey, were for the purpose of liquidating property that FDIC and RTC obtained when the agencies took control of failed banks and savings and loans.

The complaint also alleges that the couple used subsidiaries of the husband's auction company to perform work related to the auctions and failed to report to FDIC and RTC that these subcontractors were "related entities." The subsidiary companies were allegedly used to overbill the FDIC and RTC. The wife's brother-in-law, who worked for the subsidiaries, allegedly prepared and "padded" bills submitted to the two agencies, in some instances charging \$80 per hour for work that actually cost \$24 per hour.

Through the alleged scheme, the shell company was paid more than \$1 million in commissions, approximately 1 percent of the proceeds from the auctions. FDIC and RTC also paid the firm more than \$2.5 million for expenses the firm claimed to have incurred in connection with the auctions.

As the reporting period comes to a close, the OIG is close to finalizing a memorandum of understanding with the Department of Justice, under which all OIG agents will be deputized as Special Deputy U.S. Marshals. In that capacity, agents will have the authority to seek and execute search and arrest warrants as necessary in the course of any investigation they conduct. The memorandum of understanding will place the FDIC OIG among the majority of Offices of Inspector General whose agents are deputized for all investigations.

Historically, FDIC OIG agents have been required to seek deputation as needed on an individual case-by-case basis.

"Blanket deputation," as it is known in the OIG community, will enhance the efficiency and effectiveness of our operations.

Under the False Claims Act, the defendants are personally liable for up to three times the nearly \$3.6 million paid the shell company by FDIC and RTC. They also face up to \$10,000 in fines for each of the more than 2,500 false claims allegedly filed in the scheme. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 provides an additional \$5 million penalty for making false statements designed to influence the RTC and the FDIC.

Commenting on the seriousness of the alleged offenses, United States Attorney Nora Manella stated that the auctioneer had “masterminded a multifaceted fraud that allowed him to profit illegally from the savings and loan crisis and from programs designed to help women.”

---

### **Unremitted Funds Project**

A project undertaken by the Office of Investigations to assist FDIC in collecting unremitted funds due from contractors has led to significant recoveries for the FDIC. Our work in this area is a continuation of an initiative first started by the RTC OIG Office of Investigations in Kansas City.

Prior to its closure in late 1995, the RTC Kansas City Financial Service Center requested the former RTC OIG to assist in a project to collect monies due from contractors believed to be holding RTC funds. As part of that project, the Kansas City Financial Service Center sent letters to property managers, legal contractors and court appointed receivers, asking whether they were holding any RTC funds.

The names of any contractors who failed to respond after receiving three letters were referred to the OIG for further inquiry. As other offices learned of the OIG's involvement in this project, they requested similar assistance. As a result, the names of over 120 contractors were referred to the OIG for followup. OIG agents made personal visits to these contractors to determine whether they were holding any unremitted funds and, if so, to arrange for remittance of those funds to the RTC, and later the FDIC.

In response to concerns raised by FDIC officials, the FDIC OIG later expanded its efforts to target loan servicers who might be holding funds due FDIC. We did so through the use of a questionnaire, which we sent to almost 500 loan servicers who had collected funds on behalf of RTC. Through these combined initiatives, the OIG has assisted the FDIC in identifying over \$2.4 million in funds owed by former RTC contractors. To date, \$1.1 million of those funds has been recovered and arrangements are underway for remittance of the remaining \$1.3 million balance. We expect more recoveries to follow as we continue to assist FDIC in this manner.

In addition to identifying and assisting FDIC in the collection of unremitted funds, this proactive project has led to successful criminal prosecutions. For example, through our attempts to determine whether unremitted funds were owed from a court-appointed receiver, we developed information that the receiver, a New York attorney, had defrauded RTC. The attorney, who, as a result of our investigation, pleaded guilty to misappropriating RTC funds, paid \$400,000 in restitution to FDIC as part of his plea agreement. He also faces criminal fines and the possibility of incarceration at sentencing. Our investigation found that as receiver for an RTC-owned office building in New York City, the attorney made over \$268,000 in unauthorized withdrawals from RTC receivership accounts he controlled. We also found that he improperly deposited more than \$177,000 in RTC funds into his firm's trust account.

---

## Fraud Impacting Financial Institutions

---

Historically, a significant amount of our investigative work has targeted fraud or other criminal activity arising at or involving institutions controlled by FDIC. Some of the results of our cases involving financial institutions are illustrated below.

Following an OIG investigation, a Pennsylvania real estate developer was indicted on charges that he defrauded the former Bell Savings Bank, an institution formerly controlled by RTC. The indictment also charged the developer with concealing assets from the RTC. The developer was the general contractor for three residential projects financed by Bell Savings. As described in the indictment, the developer allegedly fraudulently endorsed over \$50,000 in dual payee checks that Bell Savings issued as construction loan draw disbursements. He then allegedly deposited the checks into accounts which he controlled.

Our investigation also developed evidence supporting allegations that the developer submitted false and inflated construction invoices to Bell to induce the issuance of loan draw disbursements. He also allegedly fabricated expenses reflected on settlement sheets for lot sales and, in doing so, allegedly received reimbursement for expenses he never incurred.

Another investigation involving the former Bell Savings Association led to a sizeable recovery this period. In our last semiannual report, we described an investigation with the FBI that led a Pennsylvania real estate developer to plead guilty to a 26-count indictment on charges of bank fraud, making false statements to a financial institution, and concealing assets from the RTC. As reported, our investigation found that the developer defrauded Bell Savings of over \$1.2 million in connection with construction loans he had obtained from the institution. As a result of that conviction, the developer has since been sentenced to pay restitution of over \$1 million and to serve 1 year and 1 day in prison.

A joint investigation with the FBI into the attempted acquisition of a financially troubled California bank led to the indictment of an Israeli citizen and two American security brokers on charges of wire fraud and aiding and abetting. The Israeli citizen allegedly attempted to raise the funds for the purchase of the bank through an offering of certificates of deposit (CDs). The CDs were offered, purportedly on behalf of the bank, at grossly inflated prices in an attempt to obtain brokered deposits. The two security brokers indicted in the scheme were principals of the firm that handled and promoted the CD offering. They contacted other brokers around the country and enticed them to invest in the CDs. The bank, which never authorized the CD offering, had been prohibited by FDIC from accepting brokered deposits.

In response to the offering, the brokers allegedly collected over \$7.5 million in a 2-day period. Over \$4.7 million of those funds was wired to another California bank for credit to an account held by the Israeli's attorney. The funds were purportedly to be used to purchase the CDs. The Israeli allegedly intended to use a portion of the funds to purchase the troubled institution, with the remainder to be used for his personal benefit. Through coordination with FDIC's Division of Supervision, the FDIC froze the attorney's account and all funds were ultimately returned to the investors.

After our investigation foiled the scheme, the Israeli fled to Denmark, where he was arrested for attempting a similar scheme against a large Danish bank. He was convicted in that case and was in prison at the time of his extradition to the United States.



Three individuals were indicted after engaging in a fraudulent scheme to purchase this California bank.



A \$1.1 million settlement agreement was reached this period as a result of an investigation we conducted in conjunction with the Justice Enforcement Team (JET), a task force recently established by the U.S. Attorney's Office in the District of Massachusetts. The mission of the task force is to locate hidden assets of individuals who fail to satisfy their criminal or civil financial penalties. We initiated our investigation after an FDIC attorney reported suspicions that three convicted felons were concealing their assets and lying to probation officials about their ability to pay restitution to FDIC. The court had ordered the men to pay combined restitution of \$1.5 million to FDIC after they were convicted for defrauding the former Bank for Savings in Malden, Massachusetts. As a result of their convictions, the men were also sentenced to serve 15 months in prison.

After their release from prison, the three men, two of whom were brothers, were placed on probation for a period of 2 years. During that time, they paid less than 2 percent of the restitution owed to FDIC and represented to their probation officers that they were indigent. Our investigation developed evidence suggesting that the men were far from indigent. We found that while on probation, the men transferred assets to their wives and to numerous corporations that the men actually controlled. These assets included two large apartment complexes valued at over \$24 million, and a 20 percent interest in a golf course. We also found that while her supposedly indigent husband was on probation, one of the wives was having a new home built for them in an exclusive Maine community. Another of the men lived in a \$650,000 Boca Raton condominium, which he owned jointly with his wife.

The evidence developed during our investigation was presented at a trial held in U.S. District Court, District of Massachusetts, to determine whether the men could have paid their restitution in full during their 2 years of supervised release. At that time, the judge found that the men had the means to pay, but had instead conspired to hide their assets from the U.S. Probation Office. He characterized the testimony of one of the defendants as "nothing but a tissue of lies and fabrications." In what could be an important precedent for future restitution cases, the judge further ruled that during the period of supervised release, the defendants had an "affirmative duty to marshal their assets to pay the restitution." Instead, the judge found that the defendants "aggressively undertook a scheme to conceal their assets while at the same time maximizing their value."

Following the trial, the JET prosecutors commenced a civil proceeding to seize the apartment complexes and other assets the defendants had transferred during their period of probation. The prosecutors also requested that a receiver be appointed to take control of the apartment complexes in order to prevent funds from being diverted or drained from the apartments to support the lavish lifestyles of the defendants. In order to settle the civil suit, the three men subsequently agreed to pay the full \$1.1 million in restitution to FDIC.



While living in a \$650,000 condominium that he and his wife owned in this Boca Raton complex, a convicted felon told probation officials that he was indigent and unable to pay restitution to FDIC.



Meanwhile he and two other men were concealing assets, among them, a 408-unit apartment complex in Indiana and a 280-unit apartment in Illinois, together worth over \$24 million.

---

## **"Con-schemes"**

---

Our cases frequently target schemes by individuals who defrauded their victims by purporting to be representing the FDIC or the former RTC.

In one such case, a Los Angeles man pleaded guilty to wire fraud after our investigation found he had falsely represented that he was an employee of the RTC and was responsible for selling property that RTC had seized from failed savings and loans. Our investigation found that the man had defrauded at least 12 individuals of over \$360,000 in down payments on the properties he falsely claimed to be selling. The properties included hotels, condominium complexes, retail stores and restaurants, as well as expensive residential homes in Los Angeles and Torrance, California. As instructed, the victims in the scheme, some of whom had never met the man, wire transferred their down payments to him. Most of the victims were elderly women, some of whom lost their life-savings as a result of the scheme. Some of the victims had taken out second mortgages and/or obtained lines of credit to make the down payments. One victim was forced to declare bankruptcy as a result of the fraud.

Our investigation into another "con-scheme" came to a close this period when a jury found a New Jersey man guilty of conspiracy, mail fraud and money laundering. The man, who operated a mortgage brokerage firm

with his wife, was sentenced to serve 5 years and 3 months in prison, followed by 3 years of probation, and was fined \$1,000. Although the man's wife was earlier indicted for her alleged role in the scheme, she was declared mentally incompetent to stand trial. Our joint investigation with the FBI found that the mortgage broker participated in a scheme to defraud hundreds of investors by promising them they could earn up to 16 percent monthly interest by buying foreclosed homes from the RTC and reselling the homes. None of the properties were owned by RTC and, in fact, in some instances the homes did not even exist. To lure investors to their mortgage brokerage, the couple told them that they had a contact at the RTC when, in fact, they had no such contact. The couple used fictitious RTC letterhead they had created to convince potential investors that RTC was selling the properties in question. They also told investors that buyers for the houses had been pre-approved. Investors were defrauded of over \$8 million in this manner.

---

## **Employee Cases**

---

A case we highlighted in our last semi-annual report culminated this period with a 2-week trial in which a former employee of the FDIC was found guilty on charges of conspiracy, acceptance of illegal gratuities, embezzlement, and money laundering. As a liquidation specialist in FDIC's South Brunswick, New Jersey, office, the employee was responsible for managing and selling assets FDIC acquired from failed banks. One of those assets was a marina on the New Jersey coast. The marina complex was posted as collateral for a loan acquired by FDIC when the bank failed. When the borrowers defaulted on the loan, FDIC acquired the marina.

Our investigation, conducted jointly with the U.S. Postal Inspection Service, found that the liquidation specialist accepted cash payments of \$97,000 from the eventual purchaser of the marina. The payments were made in order to guarantee the purchase. Earlier, as a result of our investigation, the purchaser pleaded guilty to making false statements to the FDIC in connection with the scheme.

In addition to accepting illegal gratuities, the liquidation specialist embezzled an insurance settlement check issued for a claim made prior to the bank's closure. The employee forwarded the \$138,500 check to a business partner, who wired the funds back to an account controlled by the employee. The employee then withdrew the funds for his personal use over a period of several months.

Another former FDIC employee was charged with embezzling federal pension funds as a result of an OIG investigation. The former employee, a Texas resident, allegedly embezzled almost \$400,000 from pension plans in Texas and Oklahoma. FDIC became the receiver/trustee of the funds as a result of the failure of financial institutions in the two states. The man allegedly used

the funds to purchase, among other items, a personal residence for \$107,000 and a BMW automobile for \$34,255. The man has already turned the car over to the government as a result of our investigation and is in the process of selling the residence he purchased with the stolen funds. It may not be so easy for him to turn over the remainder of the funds he embezzled, a portion of which he donated to his church. The church has already spent the funds on a renovation project.



A former FDIC employee used some of the funds he embezzled from pension plans under FDIC receivership to purchase this BMW. He turned the vehicle over to the government following our investigation. Shown here with the vehicle is OIG Special Agent Larry Edgar.

## OIG Organization

### OIG Strategic Goals

- 1 The OIG will develop and deliver quality and timely products that add value to the Corporation's operations.
- 2 The OIG will sustain lines of communications between OIG staff and the client to support positive working relationships.
- 3 The OIG will foster a work environment that supports, challenges, and respects its employees.
- 4 The OIG will maintain a streamlined, dynamic operation that maximizes the ability of OIG staff to perform their work.
- 5 The OIG will pursue opportunities to expand its contribution to the FDIC and the Inspector General community.

Each federal agency has an Inspector General, who helps ensure effectiveness and efficiency of that agency's operations and prevent fraud, waste, abuse, and mismanagement that could compromise agency programs and operations. According to the fiscal year 1996 joint annual report of the President's Council on Integrity and Efficiency and the Executive Council on Integrity and Efficiency, the collective efforts of federal OIGs led to \$1.1 billion in recoveries through fines and reimbursements and recommendations to agency managers, which helped to better manage \$15.1 billion. In addition, OIGs successfully prosecuted over 12,000 individuals involved in criminal acts against the government.

The FDIC Board of Directors established the FDIC Office of Inspector General on April 17, 1989, pursuant to the Inspector General Act Amendments of 1988. Since inception, three Inspectors General have served. The present Inspector General, Gaston L. Gianni, Jr., was appointed by the President and confirmed by the Senate as required by the Resolution Trust Corporation Completion Act of 1993. The Inspector General works under the general supervision of the FDIC Chairman.

The FDIC OIG's primary mission is to assist the Corporation in accomplishing its mission to provide protection for bank depositors and foster sound banking practices for more than 11,000 of the nation's banks and savings associations. The OIG is charged with independently reviewing FDIC programs through audits, investigations, evaluations, and other reviews to ensure the economy and efficiency of program operations. The OIG is also charged with making recommendations to prevent and detect fraud, waste, abuse, and mismanagement, which could jeopardize the success of FDIC's programs and mission.

To fulfill its mission, the OIG works toward five goals, developed in conformity with the requirements of the Government Performance and Results Act. These goals are outlined in the OIG's business plan for 1997 and are met by implementing and monitoring measurable performance objectives. The OIG's six internal offices pursue these goals and objectives through comprehensive nationwide programs. OIG staff are currently located in Washington, DC; Dallas, Texas; Atlanta, Georgia; Chicago, Illinois; and Irvine, California.



## Meeting the Challenge

Central to meeting all the OIG's goals and objectives is an emphasis on sustaining strong lines of communication between the OIG's clients and its staff, which promotes an open, positive working relationship. The OIG also pursues varied opportunities to enhance its communication with, and subsequently its contribution to the FDIC, the Inspector General community, and the Congress. Through ongoing communications with FDIC's Office of Internal Control Management, as well as proactively commenting on proposed Corporation policies, regulations, and legislation, the OIG impacts corporate programs and initiatives as they are being developed and can help to ensure adequate internal controls. In addition, the OIG's Office of Congressional Relations and Evaluations responds to Congressional requests for OIG reviews and information and requests from agency management. Further, the OIG's presentation of audit and evaluation reports at Audit Committee meetings provides an opportunity to emphasize major issues and findings. OIG staff participation in the President's Council on Integrity and Efficiency (PCIE) creates a strong link with the Inspector General community and an opportunity to influence the direction of IG policies. The PCIE continually examines the role of Offices of Inspector General in major federal initiatives and seeks to improve the quality of OIG operations in all federal agencies. Some PCIE groups in which the OIG participates, such as its Audit Committee, the OIG Hotline Working Group, and the Inspections and Evaluations' Round Table, develop guidance to ensure greater uniformity of practices among OIGs.

OIG participation in corporate task forces to explore solutions to agency challenges fosters a positive cooperative working relationship with FDIC management. Projects address such topics as the Millennium Project-Year 2000; FDIC's Cost Benefit Analysis Task Force; streamlining and automating time and attendance reporting; implementing changes mandated by the Electronic Freedom of Information Act Amendments of 1996; developing an electronic travel voucher system; and examining current and future agency space and building needs and options.

Table 1: **Significant OIG Achievements  
April 1, 1997 through September 30, 1997**

All Dollars in Millions	
Audit Reports Issued	63
Questioned Costs	\$ 8.6
Investigations Opened	53
Investigations Closed	73
OIG Subpoenas Issued	7
Convictions	9
Fines, Restitution, and Monetary Recoveries	\$ 4.6
Evaluations Initiated	5
Evaluation Reports Issued	6
Contractor Expiration Reviews Completed	25
Questioned Costs	\$ 4.1
Hotline Allegations Referred	30
Allegations Substantiated	4
Closed	31
Proposed Regulations Reviewed	20
Proposed FDIC Policies Reviewed	39
Responses to Requests and Appeals under the Freedom of Information and Privacy Acts	56

To encourage excellence within its own organization, the OIG attempts to foster a work environment that supports and challenges its employees and maximizes the ability of OIG staff to perform high quality work. The Offices of Audits and Investigations have initiated comprehensive planning conferences aimed at bringing regional and Washington office staff together to enhance performance and ensure consistent approaches to performing work and reporting results. In addition, OIG staff participate in a wide range of professional organizations that further meet both

organizational and personal professional development needs, including the Institute of Internal Auditors, American Institute of Certified Public Accountants, Association of Certified Fraud Examiners, Association of Government Accountants, and Federal Law Enforcement Officers Association. Internally, the OIG Information Technology Task Force recently issued an information technology plan, which culminated a year-long study of OIG information technology needs and identified the OIG's major information technology issues. A program to recruit and train undergraduate and graduate student interns in the Offices of Audits and Counsel was also carried out during the reporting period. This program fosters a commitment to continuing the development of a well trained, high-quality federal workforce for the future.

## A Look at Our Offices

The **Office of Audits** conducts full scope audits, reviews, and evaluations of corporate and receivership activities as well as residual Resolution Trust Corporation (RTC) business matters. Audits are performed at headquarters and field offices, various sites nationwide, and at FDIC contractors' facilities. Audits relate to areas of strategic importance to the Corporation and include deposit insurance; supervision and consumer affairs; financial accountability and internal controls; asset servicing and liquidation; award, administration, and oversight of contracts and agreements; corporate administration; and financial and management information systems. The office is also working closely with the U.S. General Accounting Office to assume a greater OIG role in performing the annual financial audits of FDIC funds, as required by the Chief Financial Officers Act and other legislation. The Office of Audits issued 63 reports during this reporting period, all of which are listed in Table I.2 of Appendix I.

The **Office of Investigations** carries out a nationwide program for the prevention, detection, and investigation of criminal or otherwise prohibited activity affecting FDIC or its programs. The office maintains close, ongoing working relationships with the U.S. Department of Justice, the Federal Bureau of Investigation, the U.S. Secret Service, other Offices of Inspector General, and state and local law enforcement agencies. This office has recently initiated or completed several initiatives to increase the effectiveness and efficiency of its program. For instance, under a

### Government Performance and Results Act

The OIG took a proactive role in assisting the Corporation as it prepared its Strategic and Annual Performance Plans. The Corporation is submitting these plans to the Office of Management and Budget and the Congress for the first time under the Government Performance and Results Act of 1993. The OIG analyzed the requirements of the Results Act and provided comments to management on the Corporation's draft Strategic Plan. The Corporation submitted a preliminary version of the Strategic Plan to the House Committee on Banking and Financial Services in July. The Strategic Plan and the Annual Performance Plan, which translates the Strategic Plan into current activities and related annual measurable goals, were submitted in conformance with Results Act requirements at the end of September.

## OIG Assistance to FDIC Management April 1997 - September 1997

memorandum of understanding with the Department of Justice, the OIG will receive blanket deputation for all OIG agents for a 2-year period, which eliminates the need to coordinate with the Department of Justice on a case-by-case basis for warrants and arrests. The office has also increased its training opportunities for investigators, particularly in the areas of law enforcement techniques and firearms proficiency. The office opened 53 investigations and closed 73 during this reporting period, as shown earlier in Table 1.

The **Office of Congressional Relations and Evaluations** complements audit and investigative activities with short-term reviews that are narrowly focused and generally result in reports issued to management. This office's function is to quickly conduct evaluations of specific FDIC operations and recommend improvements that enhance efficiency and effectiveness. It also responds to Congressional requests for OIG reviews and information. The evaluations are usually initiated based on requests by the Board of Directors, the Congress, OIG Hotline, and senior FDIC managers. During this semiannual reporting period, six evaluations were completed. See Appendix II for a listing of evaluation reports issued during this period.

The **Office of Quality Assurance and Oversight** (OQAO) is responsible for maintaining quality assurance programs for OIG activities; the external peer review of other OIG offices; internal coordination and external oversight of internal control activities under the Chief Financial Officers Act and the Federal Managers' Financial Integrity Act; internal and external coordination of strategic planning and performance measurement activities under the Government Performance and Results Act of 1993; and completion of expiration reviews of RTC contractors.

---

Commenting on FDIC's draft Strategic Plan to assist the Corporation in meeting the requirements of the Government Performance and Results Act.

---

Participating on FDIC's Cost Benefit Analysis Task Force to develop corporate guidance for conducting cost benefit analyses for all Corporate expenditures over \$1 million, defined by the Corporation's policy as "investments."

---

Providing feedback to developers of new Time and Attendance reporting system on system design and user requirements.

---

Participating on Corporate Operating Plan System (COPS) Project to examine FDIC headquarters' current and future building space needs and options for meeting those needs.

---

Working with the Division of Resolutions and Receiverships and Division of Finance to recover delinquent monies owed by former RTC contractors and court-appointed receivers.

---

Evaluating FDIC's methodology for identifying FDIC information technology that is not Year 2000 compatible in an audit of the Corporation's Millennium Project-Year 2000.

---

Defining, in conjunction with the Legal Division, six critical controls necessary in electronic timekeeping and billing systems.

---

Completing joint effort with management to reach management decision on more than 1,000 recommendations from RTC contractor reviews completed before RTC sunset.

---

Participating on the COPS Project to implement changes necessitated by the Electronic Freedom of Information Act (FOIA) Amendments of 1996, which changed FOIA response periods and require electronic access to certain agency records.

---

Reviewing the process leading to the Corporation's annual management report on internal controls, and providing the Chairman a report confirming that the process was conducted in a manner consistent with requirements of the Chief Financial Officers Act.

---

## Review of Regulations

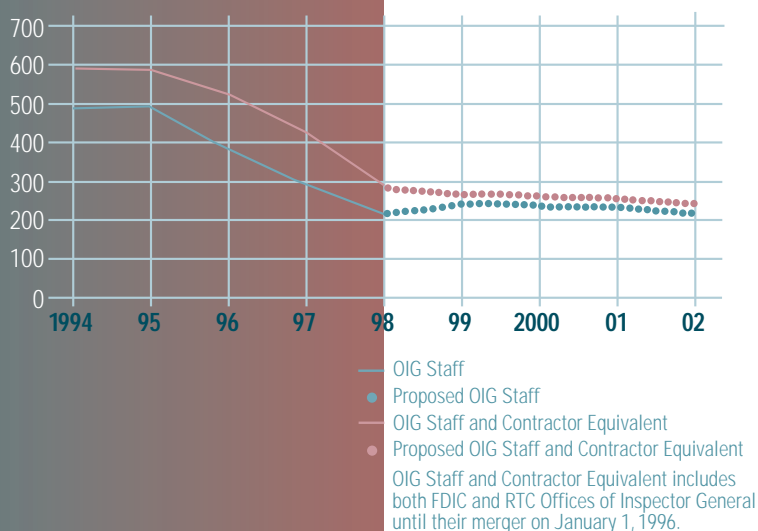
During the reporting period, the FDIC continued to intensify its systematic review of regulations and written policies as required by Section 303(a) of the Riegle Community Development and Regulatory Improvement Act of 1994 (CDRI). Section 303(a) of the CDRI, codified as 12 U.S.C. 4803(a), requires the FDIC to streamline and modify its regulations and written policies in order to improve efficiency, reduce unnecessary costs, and eliminate unwarranted constraints on credit availability. Section 303(a) also requires the FDIC to remove inconsistencies and outmoded and duplicative requirements from its regulations and written policies. During the past 6-month period, the OIG reviewed 20 regulatory and policy changes proposed by the FDIC and provided comments as necessary.

During the period OQAO provided assistance to FDIC on its draft Strategic Plan and completed 25 contractor oversight reviews as part of a joint initiative with management to complete closeouts of contractor work assumed from RTC at sunset. The office conducted an external quality control review of the U.S. Environmental Protection Agency's OIG Office of Audit and initiated a quality control review of the Board of Governors for the Federal Reserve System OIG's Office of Audit. It began quality assurance reviews in Office of Audits in anticipation of the OIG's external quality control review and completed its work with FDIC management to close more than 1,000 open recommendations remaining from contractor reviews completed before RTC sunset.

As one of the Inspector General's senior management officials, the **Counsel to the Inspector General** provides independent legal services to the OIG. Services encompass every facet of OIG operations and include performing legal research and writing opinions; preparing subpoenas for issuance by the Inspector General; and providing supportive advice and counsel on audit, investigative, and management-related topics. In addition, the Counsel reviews proposed legislation and regulations affecting FDIC. During this reporting period the Counsel and staff coordinated OIG's reviews of 20 proposed regulations and external policy statements, responded to 56 requests and appeals under the Freedom of Information and Privacy Acts, and issued 7 subpoenas.

As the operations arm of the OIG, the **Office of Management and Policy** is responsible for developing the OIG appropriations and FDIC budgets and OIG strategic and business plans; communicating OIG policies and operating procedures; managing the OIG human resources program, which includes coordinating training to meet legislatively required minimum levels; administratively overseeing OIG contracts for audits and other services; managing OIG's review of proposed corporate policies; and providing technology support to the OIG. The OIG reviewed 39 corporate policies during this reporting period. This office also

Figure 2: Office of Inspector General Staffing (1994 - 2002)





manages the OIG Hotline, which is a program designed to encourage FDIC employees, contractors, and others to report to the OIG instances of suspected fraud, waste, abuse, and mismanagement within FDIC and its contractor operations. The OIG Hotline maintains a toll-free, nationwide Hotline (1-800-964-FDIC), electronic mail address (IGHotline@FDIC.gov), and postal mailing address. During this reporting period, the OIG referred 30 new Hotline cases for review and/or investigation. These cases related primarily to allegations of employee misconduct. It also closed 31 cases, of which 4 were substantiated.

At this juncture, the OIG downsizing effort of several years has been largely completed, with estimated future staffing plans in place through 2002. The OIG proposes to reach a core staff of 220 by 2001 and beyond. Figure 2 shows past and projected OIG staffing levels through year 2002.

### **OIG Internal Management Initiatives**

**April 1997 - September 1997**

---

OIG submits funding request for fiscal year 1998; the House and Senate approve.

---

OIG connects world wide web homepage to the FDIC Intranet. ([www.ignet.gov/ignet/internal/fdic/index.html](http://www.ignet.gov/ignet/internal/fdic/index.html))

---

OIG Hotline becomes available through the Internet at [IGHotline@FDIC.gov](mailto:IGHotline@FDIC.gov); and an OIG Hotline brochure, entitled OIG Hotline & You is issued to 8,600 FDIC employees in their earnings and leave statements.

---

OIG's Information Technology Task Force issues its Information Technology Plan.

---

OIG Incentive Awards Committee makes recommendations on the awards program in the OIG.

---

OIG implements pilot program to test and evaluate the use of automated audit workpapers.

---

OIG begins a major assessment of OIG management information systems and testing to ensure Year 2000 compliance.

---

OIG reviews all OIG position descriptions to ensure they accurately reflect responsibilities and expectations.

---

## Results

As the OIG works within the framework of the Results Act, we will focus on capturing the results of our work over time. The following figures depict our progress in several areas over the past several reporting periods.

Figure 3: Reports Issued and Investigations Closed

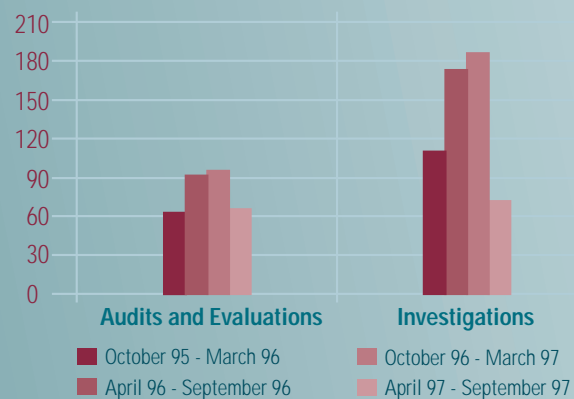


Figure 4: Questioned Costs

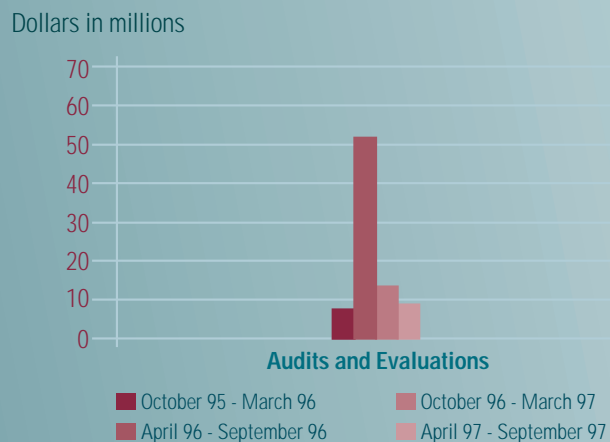
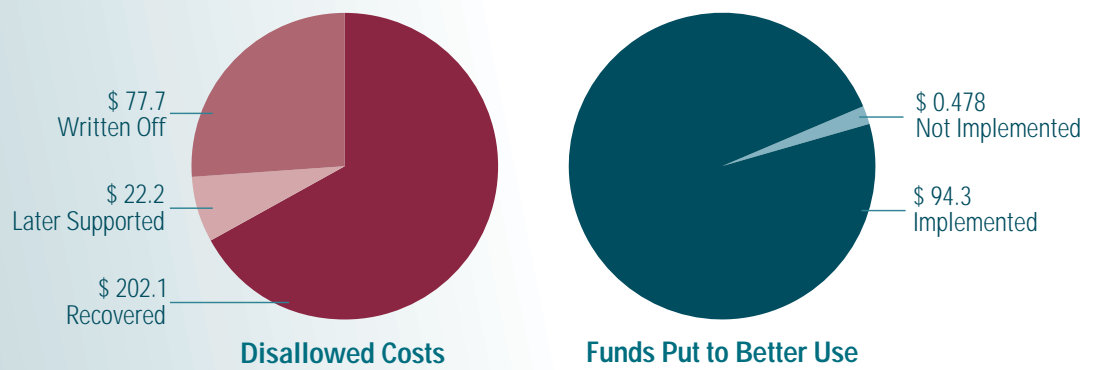


Figure 5: Fines, Restitution, and Monetary Recoveries



Figure 6: **FDIC Management Actions on OIG Monetary Benefits**

Dollars in millions



Source: Management Semiannual Reports to the Congress from October 1, 1994 through March 31, 1997

## Reporting Terms and Requirements

### Reporting Terms and Requirements

Index of Reporting Requirements – Inspector General Act of 1978, as amended	Pg
<b>Section 4(a)(2)</b> Review of legislation and regulations	40
<b>Section 5(a)(1)</b> Significant problems, abuses, and deficiencies	6-25
<b>Section 5(a)(2)</b> Recommendations with respect to significant problems, abuses, and deficiencies	6-25
<b>Section 5(a)(3)</b> Recommendations described in previous semiannual reports on which corrective action has not been completed	45
<b>Section 5(a)(4)</b> Matters referred to prosecutive authorities	26
<b>Section 5(a)(5) and 6(b)(2)</b> Summary of instances where requested information was refused	58
<b>Section 5(a)(6)</b> Listing of audit reports	50
<b>Section 5(a)(7)</b> Summary of particularly significant reports	6-25
<b>Section 5(a)(8)</b> Statistical table showing the total number of audit reports and the total dollar value of questioned costs	56
<b>Section 5(a)(9)</b> Statistical table showing the total number of audit reports and the total dollar value of recommendations that funds be put to better use	57
<b>Section 5(a)(10)</b> Audit recommendations more than 6 months old for which no management decision has been made	58
<b>Section 5(a)(11)</b> Significant revised management decisions during the current reporting period	58
<b>Section 5(a)(12)</b> Significant management decisions with which the OIG disagreed	58

### Reader's Guide to IG Act Reporting Terms

#### What Happens When Auditors Identify Monetary Benefits?

*Our experience has found that the reporting terminology outlined in the Inspector General Act of 1978, as amended, often confuses people. To lessen such confusion and place these terms in proper context, we present the following discussion:*

The IG Act defines the terminology and establishes the reporting requirements for the identification and disposition of questioned costs in audit reports. To understand how this process works, it is helpful to know the key terms and how they relate to each other.

The first step in the process is when the audit report identifying **questioned costs** is issued to FDIC management. Auditors question costs because of an alleged violation of a provision of a law, regulation, contract, grant, cooperative agreement, or other agreement or document governing the expenditure of funds. In addition, a questioned cost may be a finding in which, at the time of the audit, a cost is not supported by adequate documentation; or, a finding that the expenditure of funds for the intended purpose is unnecessary or unreasonable.

The next step in the process is for FDIC management to make a decision about the questioned costs. The IG Act describes a **“management decision”** as the final decision issued by management after evaluation of the finding(s) and recommendation(s) included in an audit report, including actions deemed to be necessary. In the case of questioned costs, this management decision must specifically address the questioned costs

by either disallowing or not disallowing these costs. A **“disallowed cost,”** according to the IG Act, is a questioned cost that management, in a management decision, has sustained or agreed should not be charged to the government.

Once management has disallowed a cost and, in effect, sustained the auditor's questioned costs, the last step in the process takes place which culminates in the **“final action.”** As defined in the IG Act, final action is the completion of all actions that management has determined, via the management decision process, are necessary to resolve the findings and recommendations included in an audit report. In the case of disallowed costs, management will typically evaluate factors beyond the conditions in the audit report, such as qualitative judgements of value received or the cost to litigate, and decide whether it is in the Corporation's best interest to pursue recovery of the disallowed costs. The Corporation is responsible for reporting the disposition of the disallowed costs, the amounts recovered, and amounts not recovered.

Except for a few key differences, the process for reports with recommendations that **funds be put to better use** is generally the same as the process for reports with questioned costs. The audit report recommends an action that will result in funds to be used more efficiently rather than identifying amounts that may need to be eventually recovered. Consequently, the management decisions and final actions address the implementation of the recommended actions and not the disallowance or recovery of costs.



## **APPENDIX I: STATISTICAL INFORMATION REQUIRED BY THE INSPECTOR GENERAL ACT OF 1978, AS AMENDED**

**TABLE I.1: SIGNIFICANT RECOMMENDATIONS FROM PREVIOUS SEMIANNUAL REPORTS ON WHICH CORRECTIVE ACTIONS HAVE NOT BEEN COMPLETED**

This table shows the corrective actions that FDIC management has agreed to implement but has not completed, along with associated monetary amounts. In some cases, these corrective actions are different from the initial recommendations made in the audit reports. However, the OIG has agreed that the planned actions meet the intent of the initial recommendations. The information in this table is based on information supplied by FDIC's Office of Internal Control Management (OICM). These 55 recommendations from 17 reports involve monetary amounts of over \$37 million. OICM has categorized the status of these recommendations as follows:

### **Management Action in Process: (27 recommendations from 8 reports)**

Management is in the process of implementing the corrective action plan, which may include modifications to policies, procedures, systems or controls; issues involving monetary collection; and settlement negotiations in process.

### **Legal Analysis: (3 recommendations from 2 reports)**

The Legal Division has been provided all necessary documentation to perform a detailed review for legal purposes. The Legal Division will be the final determinant for items so categorized.

### **Litigation: (25 recommendations from 7 reports)**

Each case has been filed and is considered "in litigation." The Legal Division will be the final determinant for all items so categorized.



REPORT NUMBER, TITLE & DATE	SIGNIFICANT RECOMMENDATION NUMBER	BRIEF SUMMARY OF PLANNED CORRECTIVE ACTIONS AND ASSOCIATED MONETARY AMOUNTS
<b>MANAGEMENT ACTION IN PROCESS</b>		
95-094 <b>Audit of the Legal Fees Paid to the Law Firm of Petit &amp; Martin</b> September 25, 1995	2	Obtain a refund from the law firm of \$18,442 for facsimile charges billed in excess of actual costs.
	3	Obtain a refund from the law firm of \$18,218 for hourly rates billed in excess of contract rates.
96-073 <b>Niagara Asset Corporation Asset Pool</b> August 8, 1996	7	Disallow \$42,825 in inappropriate disbursements and unsupported documentation.
96-103 <b>Follow-up Audit: Cost Estimate Process for Bank Resolutions</b> September 13, 1996	1	Periodically compare initial Division of Resolutions least cost estimates with current Division of Finance records of actual liquidation activity and evaluate instances where wide variances exist, for the purpose of identifying recurring causes of the variances that should be considered in future least cost determinations.
	2	Establish a systematic method for developing current and valid economic assumptions to use during the asset valuation review process, including: (1) input from all FDIC divisions involved in the resolution and liquidation process and (2) assumptions that relate to the areas in which the failing banks are located.
	3	Closely monitor the results of the new coefficients used for estimating indirect liquidation expenses and, if necessary, make additional adjustments.
96-111 <b>FDIC Health Benefits Program and Flexible Spending Accounts Administered by Aetna Life Insurance Company</b> October 8, 1996	1	Collect \$408,274 in over payments to health care providers.
	4-9	Improve Aetna claim processing, investigate potential duplicate payments and benefit errors, and obtain a refund of \$67,355 for duplicate payments and improperly coordinated claims.
	12-13	Obtain a refund of \$123,392 for credit errors, improperly processed voided transactions, and eligibility errors.
	16-17	Obtain a refund of \$25,794 for amounts withheld from providers.
	22	Reconcile accounting and claims records and provide the reconciliations to FDIC.



REPORT NUMBER, TITLE & DATE	SIGNIFICANT RECOMMENDATION NUMBER	BRIEF SUMMARY OF PLANNED CORRECTIVE ACTIONS AND ASSOCIATED MONETARY AMOUNTS
96-132 <b>RTC's Securitization Payment Retention Funds</b> November 7, 1996	1	Request master servicers to return outstanding balances or provide adequate justification for retaining those funds.
A95-HQ-012 <b>Settlement Workout Team Basic Ordering Agreements</b> June 12, 1995	5	Disallow \$39,287 that Stonehenge billed RTC for travel hours of its employees.
	6	Disallow \$11,523 in other questionable cost paid to Stonehenge.
A95-PA-023 <b>Legal Services Provided to RTC by Elkins &amp; Yount</b> September 7, 1995	1	Disallow all unsupported and inaccurate time charges in the amount of \$23,706.
	2	Disallow \$1,700 for excessive attorney time.
	3	Disallow \$92 for services billed which were not adequately detailed.
	4	Disallow all unallowable professional fees in the amount of \$971.
	8	Disallow \$250 in unallowable expenses charged to RTC.
EVAL-97-004 <sup>a</sup> <b>Federal Deposit Insurance Corporation's Contract with Shared Technologies Fairchild to Provide Telephone Service and Equipment to the Western Service Center</b> March 28, 1997	1	Disallow \$996,128 of charges not supported by the contract or industry practice, or which appear unreasonable.
<b>LEGAL ANALYSIS</b>		
A95-HQ-011 <b>RTC's Use of Kidder, Peabody &amp; Co. for Oak Tree Federal Savings Bank</b> May 23, 1995	1	Disallow fees of \$155,000 billed outside the contract effective period and determine the disallowed fees to be ratified.
<sup>a</sup> This evaluation report is not an Office of Audits report; however, it is included here because of the questioned costs it contains.		



<b>REPORT NUMBER, TITLE &amp; DATE</b>	<b>SIGNIFICANT RECOMMENDATION NUMBER</b>	<b>BRIEF SUMMARY OF PLANNED CORRECTIVE ACTIONS AND ASSOCIATED MONETARY AMOUNTS</b>
A95-KC-006 <b>Midland Data Systems' Billings for Selected Subcontractor Costs</b> March 15, 1995	1	Disallow \$3,076,422 in improperly approved subcontractor expenses and determine if the subcontractors met RTC requirements.
	2	Disallow \$1,663,371 of Midland's billings that are in excess of the amount Midland paid its subcontractors.
<b>LITIGATION</b>		
95-032 <b>Local America Bank, F.S.B., Assistance Agreement</b> March 24, 1995	5	Recover \$5,259,285 from the association for noncompliance with the tax benefits provisions of the assistance agreement.
96-014 <b>Superior Bank, F.S.B. Assistance Agreement, Case Number C-389c</b> February 16, 1996	1, 4-16	Recover \$4,526,389 of assistance paid to Superior Bank.
A94-DE-016 <b>Sale of WESAV Mortgage Corporation</b> September 15, 1994	1	Recover \$14.2 million from Rauscher and Smith Barney for RTC's losses resulting from Rauscher's and Smith Barney's negligence in the sale of WESAV.
	5	Recover \$1,469,540 from First Western for losses sustained by RTC, and for which First Western was unjustly enriched.
	6	Recover \$456,745 in brokerage fees RTC paid Rauscher for the sale of WESAV because of Rauscher's inadequate performance.
A95-DA-001 <b>TDC Billings Under Amendments 5 and 7 of the Long Term Data Processing Agreement</b> October 18, 1994	1	Disallow \$533,000, the amount billed under amendments 5 & 7, for reconciling cash and non-cash transactions.
	2	Disallow or obtain support for \$2.2 million billed contrary to amendment 5.
A95-DA-003 <b>TDC Billings for Deconversions Under the Long Term Data Processing Agreement</b> December 29, 1994	1	Disallow or obtain supporting documentation for \$1,079,268 billed for deconversions.



REPORT NUMBER, TITLE & DATE	SIGNIFICANT RECOMMENDATION NUMBER	BRIEF SUMMARY OF PLANNED CORRECTIVE ACTIONS AND ASSOCIATED MONETARY AMOUNTS
A95-DA-006 TDC Billings for CPU Time and Transactions Under the Long Term Data Processing Agreement June 22, 1995	1	Disallow \$248,759 in CPU time that was double-billed.
A95-DE-013 Distributions, Disbursements, and Income from the C.C. Palm- Oakhurst Partnership September 11, 1995	1	Seek distribution of \$398,848 in remaining assets (RTC's 50 percent share) from the Casden partner.
	3	Casden partner reimburse or show adequate support for \$322,526 to the partnership account for unsupported expenses.
	4	Casden partner reimburse or show required approvals for \$151,843 to the partnership for unapproved expenses.



**TABLE I.2: AUDIT REPORTS ISSUED BY SUBJECT AREA**

AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
<b>SUPERVISION, RESOLUTION, AND CONSUMER AFFAIRS</b>				
97-053 5-16-97	Material Loss Review - The Failure of First Trust Bank, Ontario, California			
97-055 6-27-97	Audit of the Cost of Resolution for the Bank of Hartford - Phase II			
<b>DEPOSIT INSURANCE</b>				
97-092 8-29-97	Audit of the Oversight of Newly Chartered Institutions by the Division of Supervision's Atlanta Regional Office			
<b>AWARD, ADMINISTRATION AND OVERSIGHT OF CONTRACTS AND AGREEMENTS</b>				
97-024 5-8-97	Audit of Asset Management and Disposition Services Provided to RTC by Telacu/Carpenter/RealEcon Joint Venture			
97-035 6-9-97	Audit of Legal Fees Paid [by FDIC] to the Law Firm of Rivkin, Radler & Kremer	\$455,363	\$447,161	
97-044 4-1-97	Audit of Legal Fees Paid [by FDIC] to the Law Firm of Seyfarth, Shaw, Fairweather & Geraldson	\$11,043	\$3,205	
97-046 6-4-97	Audit of Onyx Asset Management's Performance Under Standard Asset Management and Disposition Agreement 763-90-0016			
97-047 4-22-97	Audit of Legal Fees Paid [by RTC] to the Law Firm of Bliss Riordan	\$920		
97-048 6-3-97	Audit of Legal Fees Paid [by RTC] to the Law Firm of Mullin, Hoard & Brown	\$48,295	\$45,453	



AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
97-050 6-6-97	Audit of the Schedule of Debits and Credits to the Special Reserve Accounts, AmWest Savings Association, Case No. SW-017c			
97-054 5-12-97	Audit of Legal Fees Paid [by RTC] to the Law Firm of Seyfarth, Shaw, Fairweather & Geraldson	\$64,583	\$26,573	
97-057 6-4-97	Audit of Judgments, Charge-offs, Deficiencies Partnership Monitoring Agreement with Davis/Realty Financial Advisors			
97-058 6-6-97	Audit of the Schedule of Book Values of Assets Transferred and Retained, AmWest Savings Association, Case No. SW-017c			
97-061 6-23-97	Audit of the Assistance Agreement, Bluebonnet Savings Bank, FSB, Case No. SW-020c	\$787,832	\$708,570	
97-064 6-20-97	Audit of Fol-Mac Joint Venture and 1099s			
97-066 7-18-97	Legal Fees Paid by the FDIC to the Law Firm of Kaufman & Canoles	\$475	\$438	
97-067 7-9-97	Legal Fees Paid by the FDIC to the Law Firm of Small, Craig & Werkenthin	\$148	\$148	
97-068 7-8-97	Legal Fees Paid by the RTC to the Law Firm of Friedman, Rodriguez & Ferraro	\$1,989		
97-069 7-8-97	Legal Fees Paid by the RTC to the Law Firm of McDonnell Dyer	\$132,024	\$108,343	
97-070 7-8-97	Legal Fees Paid by the RTC to the Law Firm of Arter & Hadden	\$1,814	\$181	
97-071 7-8-97	Legal Fees Paid by the RTC to the Law Firm of Conant, Whittenburg & Schachter	\$21,801	\$20,917	



AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
97-072 7-9-97	Legal Fees Paid by the RTC to the Law Firm of Small, Craig & Werkenthin	\$28,042	\$4,537	
97-073 7-10-97	Legal Fees Paid by the RTC to the Law Firm of Squire, Sanders & Dempsey	\$421		
97-074 7-10-97	Legal Fees Paid by the RTC to the Law Firm of Giles & Robinson	\$31,590	\$22,861	
97-075 7-11-97	Legal Fees Paid by the RTC to the Law Firm of Kemp, Smith, Duncan & Hammond, P.C.	\$2,595	\$1,752	
97-076 7-15-97	Legal Fees Paid by the RTC to the Law Firm of Feldstein, Gelpi & Gotay	\$485		
97-077 7-21-97	Audit of RTC's Standard Asset Management and Disposition Agreement with JAMCOR			
97-078 7-18-97	Audit of the Mountain AMD Limited Partnership			
97-079 7-16-97	Legal Fees Paid by RTC to the Law Firm of Brown, McCarroll & Oak Hartline	\$19,642	\$18,312	
D97-081 7-25-97	Pattillo, Brown & Hill Billings for Subsidiary Services Under Contract 0763-93-0179-003	\$43,438	\$3,418	
97-083 7-24-97	Audit of the Special Reserve Account, Downey Savings and Loan Association, Case No. C-356	\$147,636		
97-084 8-1-97	Legal Fees Paid by RTC to the Law Firm of Holme, Roberts & Owen	\$26,950	\$25,718	
97-085 8-11-97	Legal Fees Paid by FDIC to Riker, Danzig, Scherer, Hyland & Perretti	\$27,272	\$4,436	
97-086 8-1-97	Audit of the Special Reserve Account, Franklin Federal Bancorp, Case No. SW-016c			



AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
97-087 8-11-97	Legal Fees Paid by FDIC and RTC to Liskow & Lewis	\$10,767	\$57	
97-091 8-11-97	Judgments, Charge-offs, Deficiencies Partnership Monitoring Agreement with Metec Asset Management	\$13,912		
97-093 8-18-97	Legal Fees Paid by RTC to Hershner, Hunter, Moulton, Andrews & Neill	\$3,062	\$14	
97-094 8-18-97	Legal Fees Paid by RTC to Graham & James	\$7,366	\$1,943	
97-095 8-28-97	Legal Fees Paid by FDIC and RTC to Kalish, Forrester & Torres	\$3,532	\$1,817	
97-096 8-19-97	Legal Fees Paid by RTC to Gust, Rosenfeld & Henderson	\$24,152	\$131	
97-097 9-9-97	Legal Fees Paid by FDIC and RTC to Reid & Priest	\$14,802	\$386	
97-098 8-26-97	Legal Fees Paid by RTC to Frith & Stump	\$28,234	\$4,062	
97-101 9-12-97	Legal Fees Paid by FDIC and RTC to Lorance & Thompson	\$70,548	\$49,026	
97-102 9-24-97	Judgments, Charge-offs, Deficiencies Partnership Monitoring Agreement with Asset Management Associates	\$3,972		
97-105 9-30-97	Audit of Wasserstein Perella Mortgage Capital, Inc.	\$701,160	\$291,450	
EVAL - 97-010 <sup>a</sup> 9-30-97	Review of Invoices Submitted by SECURIGUARD® INCORPORATED	\$76,892	\$76,892	
<b>ASSET SERVICING AND LIQUIDATION</b>				
97-007 7-17-97	Audit of Loans Repurchased by the FDIC from Fleet Bank			

<sup>a</sup> This evaluation report is not an Office of Audits report; however, it is included here because the questioned costs associated with this report are included in Table I.3.



AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
97-041 6-16-97	Quarterly Certificate Audit of the Merchants Bank	\$1,602	\$1,602	
97-045 4-15-97	Audit of RTC's S-Series Transaction 1993 S-2	\$2,500	\$2,500	
97-049 6-16-97	Quarterly Certificate Audit of Webster Bank, New Haven, Connecticut			
97-052 5-2-97	Audit of Receivership Terminations in the Midwest Service Center			
97-059 6-13-97	Audit of Securitization Credit Enhancement Reserve Funds for Series 1992-07	\$517,891	\$517,891	
97-060 6-16-97	Quarterly Certificate Audit of Fleet National Bank of Rhode Island (Eastland Bank & Eastland Savings Bank) and Fleet Bank of Massachusetts, N.A. (Heritage Bank for Savings)			
97-065 6-30-97	Quarterly Certificate Audit of CrossLand Federal Savings/Republic National Bank of New York			
97-080 7-17-97	Audit of FDIC Property Tax Reassessments and Refunds, Western Service Center	\$4,504,716		
A97-082 7-28-97	Potus' Investment in Finance Associates Joint Venture Partnership	\$748,674		
A97-088 8-14-97	Receivership Claims Determinations by FDIC's Atlanta Office			
97-089 8-11-97	Audit of DRR's Major Assets			
<b>FINANCIAL AND MANAGEMENT INFORMATION SYSTEMS</b>				
97-051 5-7-97	Audit of the UNIX/ORACLE Server			



AUDIT REPORT		QUESTIONED COSTS		FUNDS PUT TO BETTER USE
NUMBER & DATE	TITLE	TOTAL	UNSUPPORTED	
97-056 6-5-97	Audit of the General Examination System (GENESYS) Development Project			
97-063 6-19-97	Audit of CICS for the IBM and Amdahl Mainframe Computers			
97-106 9-29-97	Time and Attendance Processing System (TAPS) Development Project			
CORPORATE ACTIVITIES AND ADMINISTRATION				
97-090 8-11-97	Audit of the Escrow Account Maintained by Mesne Properties	\$48,935		
97-100 9-10-97	Semiannual Report of FDIC Board Members' Travel Voucher Reviews - March 1997 through August 1997			
<b>TOTALS FOR THE PERIOD</b>		<b>\$8,637,075</b>	<b>\$2,389,794</b>	



**TABLE I.3: AUDIT REPORTS ISSUED WITH QUESTIONED COSTS**

	NUMBER	QUESTIONED COSTS	
		TOTAL	UNSUPPORTED
A. For which no management decision has been made by the commencement of the reporting period.	0	0	0
B. Which were issued during the reporting period.	40 <sup>a</sup>	\$8,637,075	\$2,389,794
<b>Subtotals of A &amp; B</b>	<b>40</b>	<b>\$8,637,075</b>	<b>\$2,389,794</b>
C. For which a management decision was made during the reporting period.	40	\$8,639,148	\$2,389,794
(i) dollar value of disallowed costs.	40	\$7,895,262	\$1,692,031
(ii) dollar value of costs not disallowed.	15 <sup>b</sup>	\$743,886	\$697,763
D. For which no management decision has been made by the end of the reporting period.	0	0	0
Reports for which no management decision was made within 6 months of issuance.	0	0	0

<sup>a</sup> An Evaluation report is included in this line. The report questioned \$76,892, and all the monetary benefits were unsupported and disallowed.

<sup>b</sup> The 15 reports not disallowed are also included in the line for costs disallowed, since management did not agree with some of the questioned costs.



**TABLE I.4: AUDIT REPORTS ISSUED WITH RECOMMENDATIONS FOR BETTER USE OF FUNDS**

	NUMBER	DOLLAR VALUE
A. For which no management decision has been made by the commencement of the reporting period.	0	0
B. Which were issued during the reporting period.	0	0
<b>Subtotals of A &amp; B</b>	<b>0</b>	<b>0</b>
C. For which a management decision was made during the reporting period. <sup>a</sup>	0	0
(i) dollar value of recommendations that were agreed to by management.	0	0
- based on proposed management action.	0	0
- based on proposed legislative action.	0	0
(ii) dollar value of recommendations that were not agreed to by management.	0	0
D. For which no management decision has been made by the end of the reporting period.	0	0
Reports for which no management decision was made within 6 months of issuance.	0	0

<sup>a</sup> Does not include two reports for which a management decision was made in a prior reporting period and resulted in pro rata recognition of \$925,000 during this period.



---

**TABLE I.5: STATUS OF OIG RECOMMENDATIONS WITHOUT MANAGEMENT DECISIONS**

During this reporting period, there were no recommendations without management decisions.

**TABLE I.6: SIGNIFICANT REVISED MANAGEMENT DECISIONS**

During this reporting period, there were no significant revised management decisions.

**TABLE I.7: SIGNIFICANT MANAGEMENT DECISIONS WITH WHICH THE OIG DISAGREED**

During this reporting period, there were no significant management decisions with which the OIG disagreed.

**TABLE I.8: INSTANCES WHERE INFORMATION WAS REFUSED**

During this reporting period, there were no instances where information was refused.



## **APPENDIX II: REPORTS ISSUED BY OFFICE OF CONGRESSIONAL RELATIONS AND EVALUATIONS**

<b>REPORT NUMBER</b>	<b>DATE</b>	<b>TITLE</b>
97-006	June 3, 1997	Allegations Regarding Disclosure of Confidential Lippo Bank Information
97-007	June 5, 1997	Extensions of Term Appointments and Conversions to Permanent Positions in the Division of Administration
97-008	August 25, 1997	Renovation of Virginia Square
97-009	September 2, 1997	Disposition of Assets with Environmental Hazards
97-010	September 30, 1997	Review of Invoices Submitted by SECURIGUARD® INCORPORATED
97-011	September 30, 1997	Review of the Federal Deposit Insurance Corporation's Contract with Anstec, Inc., to Provide Local Area Network Administration and Technical Support Services



## APPENDIX III: STATISTICAL INFORMATION RELATED TO OIG COMPLETION OF RTC CONTRACTOR REVIEWS

Before RTC sunset, the OIG agreed to assume responsibility for completing the reviews of RTC contractors initiated or planned by an RTC management oversight unit. OIG work includes facilitating management's resolution of report recommendations, including resolution of the recommendations in the backlog of unresolved reports transitioned to the FDIC at January 1, 1996. During this reporting period, we reached management decision on the last open recommendation from those reports. The tables below present information related to that OIG activity.

This information is not included with audit statistics in Appendix I of this report because this work was initiated by RTC management, using agreed-upon procedures with independent public accountants, to meet management's need for contractor oversight and contract closeout.

**TABLE III.1: STATUS OF MANAGEMENT DECISIONS ON RECOMMENDATIONS CONTAINED IN RTC CONTRACTOR EXPIRATION REVIEW REPORTS ISSUED SINCE JANUARY 1, 1996**

	NUMBER OF REPORTS	NUMBER OF RECOMMENDATIONS	QUESTIONED COSTS (\$ IN MILLIONS)
Total OIG Reports Issued Since RTC Sunset	82	316	\$12.77
Total Management Decisions:			
A. Prior to This Reporting Period	24	57	\$2.15
B. This Reporting Period	21	132	\$2.07
<b>Subtotals of A &amp; B</b>	<b>45</b>	<b>189</b>	<b>\$4.22</b>
Total Questioned Costs Disallowed:			
C. Prior to This Reporting Period	13	31	\$1.84
D. This Reporting Period	22	55	\$1.12
<b>Subtotals of C &amp; D</b>	<b>35</b>	<b>86</b>	<b>\$2.96</b>
Total Without Management Decision at September 30, 1997	37	127	\$8.55



**TABLE III.2: STATUS OF MANAGEMENT ACTIONS ON RECOMMENDATIONS CONTAINED IN RTC CONTRACTOR EXPIRATION REVIEW REPORTS ISSUED SINCE JANUARY 1, 1996**

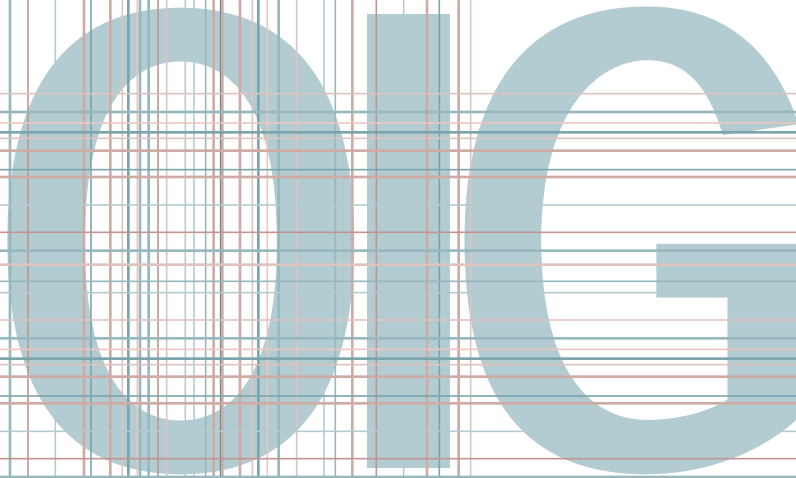
	NUMBER OF RECOMMENDATIONS	QUESTIONED COSTS DISALLOWED (\$ IN MILLIONS)
Total Management Actions Required	189	\$2.96
Management Actions Completed:		
A. Prior to This Reporting Period	41	\$1.58
B. This Reporting Period	116	\$0.87
<b>Subtotals of A &amp; B</b>	<b>157</b>	<b>\$2.45</b>
Management Actions Remaining To Be Completed at September 30, 1997	32	\$0.51

**TABLE III.3: STATUS OF MANAGEMENT ACTIONS ON RECOMMENDATIONS CONTAINED IN RTC CONTRACTOR EXPIRATION REVIEW REPORTS ISSUED BEFORE JANUARY 1, 1996<sup>a</sup>**

	NUMBER OF RECOMMENDATIONS	QUESTIONED COSTS DISALLOWED (\$ IN MILLIONS)	OTHER DISALLOWED COSTS (\$ IN MILLIONS)
Total Management Actions Required	1,545 <sup>b</sup>	\$85.98 <sup>b</sup>	\$27.30
Management Actions Completed as of March 31, 1997	1,457	88.79	\$12.60
Management Actions Remaining to be Completed as of September 30, 1997	88	\$15.66	\$14.70

<sup>a</sup> Statistics provided by and derived from FDIC Office of Internal Control Management.

<sup>b</sup> Total Management Actions Required as initially established pursuant to a joint OIG/management action plan. Management has identified retroactive adjustments not reflected in the total. We show those adjustments as Management Actions Completed.



Design and Production:  
**Division of Administration**  
Design Group

**For additional copies or information,**

**contact:**

**Federal Deposit Insurance Corporation**

**Office of Inspector General**

**801 17th Street, NW**

**Washington, DC 20434**